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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935.

No. 178

GREAT NORTHERN RAILWAY COMPANY,
Petitioner,

vs.

J. J. WEEKS, STATE TAX COMMISSIONER; J. M. BAILLIE AS AUDITOR and L. T. HALVORSON AS TREASURER OF BARNES COUNTY, et al., all of the STATE OF NORTH DAKOTA,
Respondents.

BRIEF ON BEHALF OF PETITIONER.

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St. Paul, Minn.

November 2, 1935.

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GREAT NORTHERN RAILWAY COMPANY,
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vs.

J. J. WEEKS, STATE TAX COMMISSIONER; J. M. BAILLIE as Auditor and L. T. Halvorson as Treasurer of Barnes County; G. A. Gilbertson as Auditor, W. D. Conway as Treasurer and Bert M. Salisbury as Auditor-elect of Benson County; Ole Colbornson as Auditor, Sam H. Wilson as Treasurer, C. E. Hurst as Auditor-elect and Arlan Stair as Treasurer-elect of Bottineau County; H. F. Magedanz as Auditor, Jerry Donovan as Treasurer and Thomas P. Borgen as Treasurer-elect of Burke County; F. Ford Doherty as Auditor, C. A. Baumgartner as Treasurer and Paul H. Eddy as Treasurer-elect of Cass County; Otto Rasmusson as Auditor and A. A. Wilson as Treasurer of Cavalier County; John A. Dawe as Auditor, H. J. Oberman as Treasurer and Harry Bjornstad as Treasurer-elect of Dickey County; R. H. Lynch as Auditor, O. A. Steffler as Treasurer, Myrtle Skabo as Auditor-elect and Albert T. Heide as Treasurer-elect of Divide County; S. W. Lyman as Auditor, Hugh Peoples as Treasurer and S. K. Haugland as Auditor-elect of Eddy County; J. B. McWethy as Auditor, M. P. Roberts as Treasurer and Alice Cole as Treasurer-elect of Foster County; Martin O. Haugen as Auditor, John Sandbek as Treasurer and Albert Brenna as Treasurer-elect of Grand Forks County; P. A. Melgard as Auditor, R. J. Howden as Treasurer, R. J. Howden as Auditor-elect and H. B. Nelson as Treasurer-elect of Griggs County; E. W. Olson as Auditor

and Oscar R. Fisher as Treasurer of McHenry County; Arne Tollefson as Auditor, Oluf Erickson as Treasurer and O. M. Fritsvold as Treasurer-elect of McKenzie County; F. J. Haines as Auditor, Nels Hofland as Treasurer, M. L. Glarum as Auditor-elect and Sadie Hofland as Treasurer-elect of Mountrail County; Peter Jorgenson as Auditor and J. J. Schindele as Treasurer of Nelson County; Wm. W. Felson as Auditor, J. H. Hannesson as Treasurer and Norval W. Hodgson as Treasurer-elect of Pembina County; O. A. Spillum as Auditor and O. T. Tofsrud as Treasurer of Pierce County; J. O. Peterson as Auditor and F. J. Burckhard as Treasurer of Ramsey County; C. E. Colcord as Auditor, W. C. Budke as Treasurer, W. E. Coutts as Auditor-elect and Einar Johnson as Treasurer-elect of Renville County; George J. Fischer as Auditor, Karl L. Mikkelson as Treasurer and Einar Vohnson as Treasurer-elect of Richland County; Jas. H. Penny as Auditor, Allister McKay as Treasurer and E. M. Anderson as Treasurer-elect of Rolette County; R. W. Safstrom as Auditor and H. O. Webster as Treasurer of Sargent County; G. J. Mustad as Auditor, Florence Carlson as Treasurer and Ella B. Johnson as Treasurer-elect of Steele County; A. T. Mooney as Auditor and John Gang as Treasurer of Towner County; Gerhard D. Olson as Auditor and Thomas P. Strand as Treasurer of Traill County; W. J. LaMarre as Auditor and Benj. A. Gudajtes as Treasurer of Walsh County; A. G. Torgerson as Auditor and Bert A. Balerud as Treasurer of Ward County; Otto G. Krueger as Auditor and Edith Darcy as Treasurer of Wells County; Morten Mortenson as Auditor and Oscar N. Lee as Treasurer of Williams County, all of the State of North Dakota,

Respondents.

BRIEF ON BEHALF OF PETITIONER.

The petition filed by the Great Northern Railway Company seeking a review on a writ of certiorari of the judgment of the United States Circuit Court of Appeals for the Eighth Circuit in cause number 10221 in equity, entitled Great Northern Railway Company, Appellant vs. J. J. Weeks, State Tax Commissioner, et al, Appellees, was granted by this court on October 14, 1935.

I.

THE OPINIONS OF THE COURTS BELOW.

The opinion of the District Court of the United States for the District of North Dakota has not been officially reported but the decree appears at page 53 of the record.

The opinion of the United States Circuit Court of Appeals for the Eighth Circuit dated April 25, 1935, is reported in *Great Northern Railway Company vs. Weeks, State Tax Commissioner, et al,* 77 F. (2d) 405, and appears on pages 310 to 326 of the record.

II.

JURISDICTION.

The judgment of the Circuit Court of Appeals for the Eighth Circuit was entered on April 26, 1935 (R. 327) less than three months prior to the date of application for the writ of certiorari in this court (U. S. Code, Title 28, Sec. 350).

The jurisdiction of the Supreme Court is invoked under paragraph A of Section 240 of the Judicial Code, as amended and re-enacted by the Act of February 13, 1925 (U. S. Code, Title 28, Sec. 347).

Federal Jurisdiction exists under Section 41(1) of the Judicial Code covering diversity of citizenship. Plaintiff is a cor-

poration organized under the laws of Minnesota and defendants are all citizens and residents of North Dakota. The amount or value in dispute excluding interest and costs exceeds the sum or value of $3,000.00 as to each of the defendants. Plaintiff alleged that the assessment and levy in question violate the Constitution and Laws of the United States in that they would take plaintiff's property without due process of law and impose an arbitrary and unreasonable burden on interstate commerce.

Equity jurisdiction is based upon the fact that there is no adequate remedy at law, which is not seriously disputed. The lower courts did not question their equity jurisdiction.

Wilson County Collector, et al. v. Ill. So. Ry. Co., 263 U. S. 574, 44 S. Ct. 203.

Appeal to the Circuit Court of Appeals was taken under Section 225(a) of the Judicial Code.

III.

STATEMENT OF THE CASE.

This is an action in equity brought in the United States District Court for the District of North Dakota by the Great Northern Railway Company, petitioner herein, against 83 tax collecting officers of the state and of various counties of North Dakota, respondents herein, to contest an assessment of $78,832,888 by the State of North Dakota against the property of the petitioner Great Northern Railway Company for the year 1933 and to restrain the collection of a tax levy of $1,508,352.34. The trial was by the court and decree was rendered against petitioner, plaintiff below, and in favor of the respondents, defendants below. An appeal from said decree was taken

by petitioner to the Circuit Court of Appeals for the Eighth Circuit, which affirmed the decree of the district court.

The constitution and laws of North Dakota require that all property including that of railway companies be assessed "at its true and full value in money", Section 2122, Supplement to 1913 Compiled Laws, 1913-1925. For the complete language of the constitution and laws of North Dakota on this subject see paragraph IV of the Complaint (R. 3, 5).

At the average market price for the year 1932 immediately preceding the assessment, the total aggregate value of all of the petitioner's stocks and bonds was $296,301,177.00 (Ex. B, R. 251). Of this amount the state agrees that 30.29% represented the value of non-operating assets not forming any part of the railroad system (Ex. I, R. 265). This leaves the sum of $206,551,551.00 as the value of the entire railroad system as indicated by current stock and bond prices.

The net railway operating income for the three years preceding the assessment, capitalized at 6%, produces an "earnings value" for the entire railroad property of $199,291,550.00 (Ex. 22, R. 246). Careful analyses of future earnings possibilities indicate that there is no reason to expect that the property will ever earn more than 7% on a system value of $200,000,000 (R. 65-70; 121-122).

Less than 1/7 of the entire physical plant (as measured by reproduction cost) is located in North Dakota (Ex. N, R. 273). This 1/7 of the plant had less than average traffic density and originated less than an average amount of traffic (Exs. 13, 14, R. 241). A comparison of net earnings, computed by what we believe to be a scientific and accurate method indicates that the property in North Dakota had less than 1/8 of the total net earning capacity of the system (Ex. 12, R. 237).

These facts indicate an actual commercial value for the property in North Dakota in 1933 of something like $25,000,000, while the assessment was $78,832,888.00. This assessment is nearly 40% of the actual commercial value of the entire system as indicated above, while only 1/7 or ⅛ of the system value is actually located in North Dakota.

It will be noted that the assessment appears to be a computed sum in odd dollars and not an estimate in round figures. The only explanation in the record for the precise amount of the 1933 assessment was the fact that it was identical as to amount per mile with the assessment for the prior year 1932 (R. 81), which in turn had been brought down with only a 5% reduction from the assessment for the boom year 1929 (Ex. O, R. 275). In other words, the 1933 assessment appears to have been an inheritance from the past.

Upon the trial the state attempted to support a valuation of at least the amount of $63,307,629.00 (which is about $15,000,000 less than the assessment) by certain computations of value (Ex. P, R. 277). For the excess in the assessment above the various values computed by the state, there is not even a pretense of justification in the entire record except the allegations in the answer that it was a matter of "judgment".

Both the 1932 assessment (which was adopted for 1933) and the 1933 value of $63,307,629.00 computed by the state far exceed the figure of $25,000,000 which we have suggested above as a sound commercial appraisal. Our explanation of this astonishing difference is first, that the state gives controlling weight to earnings and stock and bond prices of the boom years 1927, 1928 and 1929, and thereby assesses values of the pre-depression boom period which had long before ceased to exist; and second, that the state's computations not only value the property actually located in North Dakota but an additional

fifteen or twenty million dollars worth of terminals and mountain construction actually located in other states; and third, that some $15,000,000 is added without any explanation or justification.

The contention that property actually located in other states is included in the North Dakota assessment is supported by the fact that while North Dakota contained only 13.85%, or less than 1/7 of the physical plant, and while this portion of the physical plant had less than average traffic density and use value, North Dakota nevertheless assesses 18.34% of the system value. She has assessed not only the 13.85% actually located in North Dakota but an additional 5% located outside. This is accomplished by the use of certain mileage prorates of system value, which spread terminal values and mountain construction over the intermediate prairie states. It is (1) the assessing of pre-depression values which no longer exist, (2) the assessing of terminal values and mountain construction outside the state, and (3) the arbitrary addition of $15,000,000 without any pretense of justification which bring the total assessment up to $78,832,888.00.

The courts below held that it lay within the broad discretion of the taxing authorities to adopt such methods of valuation as this and that the court had no power to correct them; and that not even the entirely unjustified excess of $15,000,000 in the assessment, above actual value, would entitle the taxpayer to relief, in the absence of other proof of an actual fraudulent intent. Judge Sanborn stated that while he had no doubt that the property was overvalued, he felt that the power of the court had been so "circumscribed" by decisions of this court that it had no power to grant relief.

The Circuit Court of Appeals also held that *it was not sufficiently proven as a fact* that the taxing authorities had based

their assessment upon earnings and stock and bond prices of 1927-1931, or that they had in fact used the mileage prorates in apportioning system value to North Dakota. While the pleadings *specifically admit* that *both* of these methods of computation were used, the actual assessment varied by a few dollars from the precise result of these computations. The Circuit Court of Appeals seems to have held in effect that methods of computation resulting in doubling or trebling the actual value of the property, and in assessing fifteen or twenty million dollars worth of outside terminals may be used with impunity, so long as the taxing authorities add or subtract a few dollars, as an act of "judgment", before placing the amount on the assessment rolls.

Our contentions are:

(1) That the actual use by the Board of Equalization of the pre-depression figures and of the mileage prorates, is conclusively established by the evidence and admitted in the pleadings; that these methods trebled the actual value of the property; that they resulted in levying a large part of the assessment against pre-depression values which had ceased to exist and that they levied nearly 1/3 of the assessment against property actually located outside the state; and that after computing a value by such methods as this, the addition or subtraction of a few dollars before entering the amount on the assessment rolls affords no immunity.

(2) That methods resulting in the assessment of pre-depression values and out-state properties and in determining values of an obsolete period and of properties located in other states, and the further addition of $15,000,000 arbitrarily, are not within the discretion of the taxing authorities, but are subject to correction or control by the courts.

(3) That an admitted over-valuation of $15,000,000, and a confessed inability to justify it on any rational basis is in itself sufficient to show that the assessment must have been irrational and therefore arbitrary, and calls for relief without any other proof of fraudulent intent or improper method.

We know of no decisions of this court which so "circumscribe" the power of the lower courts that they cannot give relief in such a case; on the contrary we believe that several decisions of this court require that relief be granted under these conditions. In the case of *Rowley v. Chicago & North Western Ry. Co.*, 293 U. S. 102; 55 S. Ct. 55, and we think in every other case in which railway assessments have been sustained by this court, some sort of a computation had been made by the tax authorities and offered in evidence, or some sort of an attempted justification of the amount of the assessment had been made, indicating that taxing authorities had at least made an attempt in good faith to determine a value by some process which they considered rational. We believe this to be the first railroad tax case ever presented to this court, where the defendants attempted to justify the assessment and virtually confessed their inability to discover any rational process by which a valuation equal to the assessment could be computed. In this case the defendants' tax expert said that he had spent months of study on the matter and that "in all that time, I was not able to find any method of computation that would produce a value to North Dakota equal to the assessment for 1933 by any usually accepted method" (R. 190). In this respect, we submit that this case presents a situation which has never before been passed upon by this court. In addition to this, we believe that the pleadings themselves require a finding of fact that the assessment was based upon pre-depression values and mileage prorates; and a conclusion of law that such methods, when they re-

sult in trebling the value of the property, are not within the discretion of the taxing authorities.

IV.

SPECIFICATIONS OF ERROR.

(1) The Circuit Court of Appeals erred in failing to find that the assessment was more than double the actual value of the property and in failing to set aside the assessment on that ground.

(2) The Circuit Court of Appeals erred in permitting a range of discretion to the Tax Board sufficient to allow it to substantially ignore depression values and reduced economic levels and to base its assessment upon boom period values.

(3) The Circuit Court of Appeals erred in holding that plaintiff, in addition to proving the use of mileage prorates, must negative the use of any other possibly lawful method.

(4) The Circuit Court of Appeals erred in failing to find that the use of a wrongful method or arbitrary action was sufficiently established by the plaintiff's evidence of excessiveness plus the unsuccessful attempt of the state to justify the assessment; by the confession of the state's only witness that the assessment was 25% in excess of value computed by the "best and most accurate method", and that he knew of no method by which it could be justified.

(5) The Circuit Court of Appeals erred in holding that there is no basis for finding that property without the state has been assessed, unless the Board of Equalization adopted the "exact result" of a computation which included such outside values.

(6) The Circuit Court of Appeals erred in holding that there was no evidence of any deliberately arbitrary or wrongful assessment concerning years prior to 1933.

(7) The Circuit Court of Appeals erred in holding that any unlawfulness in the 1932 assessment was not necessarily carried over when the same assessment was adopted for 1933.

(8) The Circuit Court of Appeals erred in holding that it was not sufficiently established by the pleadings and evidence, that mileage prorates were in fact used in making the assessment, and that the Board of Equalization was guided or largely influenced by such computations.

(9) The Circuit Court of Appeals erred in holding that the proof of unlawfulness in the mileage prorate method of assessment depended upon proof that the only approximately true method of allocation was one based on "expense of operation".

(10) The Circuit Court of Appeals erred in holding that there is any evidence in this case that a 4% rate for capitalizing earnings would have been justified in 1933 and in failing to hold that 7% was not the minimum rate permissible under the evidence.

(11) The Circuit Court of Appeals erred in failing to find that the State of North Dakota by the use of mileage prorates had assessed many millions of dollars worth of property located in other states.

(12) The Circuit Court of Appeals erred in affirming the decision of the District Court and in entering judgment against the petitioner and in favor of the respondents.

(13) The Circuit Court of Appeals erred in not entering judgment in favor of the plaintiff as prayed for in the complaint.

V.

ARGUMENT.

Points Relied Upon.

A. The adoption of a prior year's assessment for 1933, the use of five years earnings and stock and bond prices to determine system value and the apportionment of system value to North Dakota by the use of mileage prorates were not only proven but were specifically admitted by the pleadings.

1. *The precise amount of the 1933 assessment was fixed by that of the 1932 assessment, which was adopted for 1933.*

2. *The amount of the 1932 assessment as originally made and, therefore, as adopted in 1933, was determined from earnings and stock and bond prices of the years 1927 to 1931 and by the use of mileage prorates of system value.*

B. In basing the assessment upon earnings and stock and bond prices of 1927 to 1931, the Board was in effect assessing values of an obsolete period which were no longer in existence in 1933.

C. Of the total amount of the assessment, approximately $20,000,000 was levied against properties outside the state and beyond its jurisdiction.

1. *The North Dakota trackage consists largely of relatively cheap branch lines. The more valuable terminals and more costly mountain construction are located outside the state.*

2. *The outside terminals and costly mountain construction, while concentrated in short mileage contribute as*

much to transportation service and to system value in proportion to cost and volume of plant as do the cheaper portions of the road where the same investment is spread over more miles.

3. The right to assess and tax each portion of a railway system belongs solely to the state where that portion is located.

4. The factors used in the North Dakota computations unlawfully credit to North Dakota values of terminals and mountain construction actually located in other states.

D. Where the use of unlawful methods by the taxing officers has been shown, it is not incumbent upon the taxpayer to submit a proper method of computation or to prove the correct amount that is due.

E. Even assuming that no wrongful methods were shown and that there was no evidence whatever as to what methods were used, the facts that the assessment is treble the current value of the property and that the defendants confess their inability to justify it by any rational process are sufficient to prove arbitrary action.

F. The economic emergency does not justify the violation of the statute requiring the assessment of property at its full and true value in money.

A.

The adoption of a prior year's assessment for 1933, the use of five years earnings and stock and bond prices to determine system value and the apportionment of system value to North Dakota by the use of mileage prorates were not only proven but were specifically admitted by the pleadings.

The question whether these methods would be unlawful is, of course, wholly irrelevant in this case unless it is first shown

that they were in fact used in determining the assessment. If they were not used, it is immaterial whether their use would be unlawful.

The entire opinion of the Circuit Court of Appeals consists of a labored effort by the court to show that, in spite of the specific admissions in the pleadings that these methods had in fact been used, nevertheless their use is not sufficiently shown. It is necessary, therefore, to first resolve this question, as to whether a prior year's assessment was in fact adopted for 1933 and as to whether five years earnings and stock and bond prices and mileage prorates were in fact used in determining the assessment.

1. *The precise amount of the 1933 assessment was fixed by that of the 1932 assessment, which was adopted for 1933.*

Paragraph X of the Complaint (R. 8) alleges "said Board of Equalization * * * adopted the 1932 assessment as and for its 1933 assessment and made no deduction or decrease whatever except $17,136.00 which was due to the removal of a small amount of plaintiff's trackage in North Dakota. The assessment per mile remained the same as for 1932 and the total assessment for 1933 was $78,832,000.00".

Paragraph G of the Answer (R. 26) which replies to paragraph X of the Complaint, does not deny this but alleges that the Board had statistics and other evidence of value before it in 1933, and that the assessment as actually adopted represented its honest judgment as to value.

The assessment is in odd dollars and not in round figures. It clearly appears to be the result of some kind of a mathematical computation or process and not of a rough estimate or guess. The amount is the *exact amount* which would be reached by

multiplying the 1933 mileage by the 1932 assessment per mile (R. 81). No other computation by which that precise figure might have been produced is shown or even hinted at. The allegation of the Complaint that the Board in 1933 adopted the 1932 assessment as and for its 1933 assessment is not denied. The allegations in the Answer that the Board also had other evidence before it and that the amount represented its honest judgment of the value, are in no way inconsistent with our contention that the method by which the precise amount of $78,832,888.00 with its odd dollars was arrived at was by adopting the assessment of 1932.

Various computations of value made after the assessment, and made for use as evidence in this suit, were offered by the defendants in its Exhibit P, but all of these computations are many million dollars short of the assessment. This Exhibit P was prepared by Mr. Baker, a tax specialist employed by the state, and for thirteen years a Deputy Tax Commissioner of the state, who testified that he had spent several months in preparing the exhibits and that "in all that time I was not able to find any method of computation that would produce a value to North Dakota equal to the assessment for 1933 by any usually accepted method" (R. 190).

He also testified "I believe it is correct that schedule 4 on Exhibit P showing the five factor ratio is the one which is advocated by the state as the fairest basis of allocation. That shows the 1933 assessment to be 24½% in excess of my computed value by the composite method in schedule 4" (R. 189). The computed value just referred to was $63,307,629.00 while the assessment was $78,832,888, an excess of $15,500,000 (Exhibit P).

It thus appears that there is no computation of value which will account for the amount of the 1933 assessment, except by applying 1932 assessment figures to the 1933 mileage.

Notwithstanding all this, the Circuit Court of Appeals finds "that there is no evidence as to how the Board reached its result in 1933 or prior assessments". We submit that any one who remains in doubt after this showing as to how the precise amount of the 1933 assessment was arrived at is guilty of a hair-splitting refinement which has no foundation in sound principles of logic.

In *Pennsylvania Railroad Company v. Jacoby & Co.*, 242 U. S. 89, 37 S. Ct. 49, the railroad company was attacking a reparation award of the Interstate Commerce Commission which, like the assessment in question here, was presumed to be lawful. The proof consisted simply in showing that the amount of the award was identical with the amount of a computation contained in a certain Exhibit 10, which had been introduced before the Commission by one of the parties, and which the court held would be an unlawful method of computation.

In that case the railroad company had not produced in court the entire record made before the Commission. It appeared that the Commission had had before it, evidence other than that which was produced in court, and the railway company failed to negative the possibility that some of the other evidence might have been sufficient to justify the award by some lawful method of computation. For this reason, the plaintiff took the position, which the Circuit Court of Appeals took in our case, and urged that under the presumption of lawfulness, the railway company's attack upon the award was inadequately supported. This court said on page 99:

> "It is urged that the testimony before the Commission is not all in the record, and that for aught that appears the Commission may have reached its conclusion and awarded damages upon other and competent proofs, and it is insisted that the coincidence of the amount as award-

ed and the amount ascertained by the use of the percentages contained in the tables may not necessarily have controlled the action of the Commission. But it is difficult to reach the conclusion that the Commission could have arrived at the result so exactly corresponding with the one obtained by the use of the percentages shown in the tables, except by actually using them to ascertain the sum which is exactly the amount resulting from their application. The Commission might have approximated the same result by using other and legal means to ascertain the damages sustained, but when it is demonstrated that the use of the percentages precisely produces the amount awarded to the dollar and cent, it seems almost mathematically certain that the result could have been reached in no other way. At least, we think that the testimony was in such shape that, as we have already said, the Company was entitled to the specific request upon this subject submitting the matter to the jury."

We submit that under this decision, the Circuit Court of Appeals was mistaken in assuming that the identity of the 1933 assessment per mile with that for 1932 was not evidence of the method by which the 1933 assessment was computed, and in stating that there was no evidence as to how the Board reached its results in 1933. In the absence of anything else in the record tending to cast a doubt upon this conclusion, we submit that it is controlling.

It follows that if we are to determine how the amount of the 1933 assessment was originally obtained, we must go back to 1932 when that amount was first computed.

2. *The amount of the 1932 assessment as originally made and, therefore, as adopted in 1933, was determined from earnings and stock and bond prices of the years 1927 to 1931 and by the use of milage prorates of system value.*

Upon this point we have the specific admission of the state in paragraph G of its Answer (R. 26), which reads as follows:

> "Answering Paragraph X of plaintiff's Complaint, the defendant admits that in the year 1932 the State Tax Commissioner did present to the State Board of Equalization computations based upon a determination of the system value of the railroad by the use of a composite of the average stock and bond values of the plaintiff for a period of *five years preceding the assessment*, and the average value ascertained by capitalizing net earnings *for five years preceding the assessment* and by applying and allocating such system value to the State of North Dakota upon the basis of the five factors set forth in Paragraph IX of the Complaint, which said formula produced a value of $76,115,715.00; that he also made an allocation of the same system value to North Dakota by another method, using for the purpose of allocation only factors numbered 3, 4 and 5 in said list which produced a value of $79,417,825.00. In addition thereto defendants allege that the Tax Commissioner presented the computations based upon a third method of allocating the system value by which he applied the average of the factors numbered 1, 3, 4 and 5 in the above list which produced a valuation of $80,671,790.00. Defendants further allege that *upon this evidence* and upon all other evidence and matters of common knowledge before it the Board did in the year 1932 fix the valuation of plaintiff's property in North Dakota at $78,850,024.00." (Italics ours).

These three computations of $76,115,715.00, $79,417,825.00 and $80,671,790.00, have an arithmetical average of $78,735,110.00. The 1932 assessment of $78,850,024 is very close to this arithmetical average.

It will be noted that paragraph G just quoted states that the system value was allocated to North Dakota "upon the basis of the five factors set forth in paragraph IX of the Complaint",

and also upon the factors numbered 3, 4 and 5 and the factors numbered 1, 3, 4 and 5 in said list. The factors referred to in paragraph IX of the Complaint (R. 8) are as follows:

"(1) Miles of all track.

(2) Amount of physical property as measured by cost of reproduction less depreciation.

(3) Cars and locomotives moved one mile.

(4) Tons of freight and passengers moved one mile.

(5) Gross earnings, the gross earnings in North Dakota being computed by adding to the revenues in North Dakota from intrastate traffic a proportion of the revenue from all interstate traffic passing into or through North Dakota equal to the proportion which the miles of track in North Dakota used for moving such traffic bore to the total miles of track used for moving such traffic."

It will also be noted that paragraph G above quoted states that the system value was determined from earnings and stock and bond prices "for a period of five years preceding the assessment". The assessment here referred to is the 1932 assessment and the five preceding years were the years 1927 to 1931, inclusive.

The Circuit Court of Appeals makes the amazing finding that in spite of this admission in the Answer, it is not sufficiently shown that the methods of computation referred to were used in making the assessment of 1932. The *sole basis* for this strange finding, seems to be the fact that the assessment was not in the *exact amoun* of any one of the three computations, nor in the exact amount of their arithmetical average.

The trial court had made a finding that the Board "never has adopted the *exact result* of any of said tables, formulae or methods of computation of railroad valuations" and the Cir-

cuit Court of Appeals said "if this finding is sustained by the evidence, there is no basis for the issue that out-state property is included in the assessment." In other words, it is held that unless the "exact result" of the unlawful computation is adopted as the assessment, there is no basis for contending that it was used at all, or that any unlawful result was accomplished.

The court holds in effect that even though the Board makes its computations by methods which would tax values no longer in existence, and which would tax out-state property, and which would be unlawful, it can immunize the assessment against attack by adding or subtracting a few dollars before entering the amount upon the assessment rolls. To us this is a most astonishing conclusion. The Circuit Court further says "we think appellant has failed to establish that the Board was guided by or was largely influenced by the use of any particular method, and, therefore, is in no position to urge the contention that property outside the state has been brought into this assessment". The court further says "there is no evidence of what use was made by the Board of any formula either in 1933 or prior years; that there is no evidence as to how the Board reached its results in 1933 or prior assessments".

In view of the specific admissions in the Answer, we submit that this is a most amazing conclusion. The holding seems to be that unless the wrongful formula is officially "adopted" by some resolution of the Board declaring that that is its sole official method of computation, or unless the assessment is in the exact amount of some one of these computations, the court will presume that the Board was not "guided" or was not even "largely influenced" by the use of the computations, but that it had some other secret method or formula known only to itself, and which the court will presume to have been lawful, by which the assessment was reached.

The taxpayer must assume a double burden. In addition to *affirmative* proof that the assessment was determined by unlawful methods, he must submit *negative* proof that it was not determined by lawful methods.

The Board's own expert witness, Mr. Baker, testified that after several months of study, he had been unable to discover any lawful method or formula which would support the assessment, and none was known to him (R. 190). Annual reports of the State Tax Commissioner have stated that it had been the practice for many years to fix the assessments by the use of these particular methods. These reports are not in the record but they are public documents of which the courts will take judicial notice. We quote from two of these reports in Appendices A and B of this brief. All of the computations submitted by the state in Exhibit P, in support of the assessment, are based upon these methods or some combinations of them. There is no suggestion in the record that any other method of computation was ever known to or considered by the state. Paragraph G of the Answer which admits the use of these computations does not suggest any other specific methods which were or might have been used. In view of all this, we submit that the Circuit Court of Appeals was plainly in error in stating that "appellant has failed to establish that the Board was guided by or was largely influenced by the use of any particular method" and in stating "that there is no evidence as to how the Board reached its results in 1933 or prior assessments".

The court suggests that we might have summoned the members of the Board as witnesses. However, in *C. B. & Q. R. R. Co. v. Babcock*, 204 U. S. 585, 27 S. Ct. 326, this court held that members of the Board have the immunity from examination of

jurors if not of judges and cannot be called for examination as to their mental processes. In view of this decision, it seems very doubtful whether we could have called the members of the Board as suggested by the Circuit Court of Appeals. But assuming that we had called them, and they had testified that they had made three computations as set forth in paragraph G of the Answer and had then adopted a "judgment" figure based upon these computations and upon other general knowledge, we submit that this would have proved no more than is already admitted in the answer, and that it would have been sufficient for our case. Paragraph G of the Answer (R. 27) says "Defendants further allege that *upon this evidence*" (the three computations based upon five year figures and mileage prorates) "and upon all other evidence and matters of common knowledge before it, the Board did in the year 1932 fix the valuation of plaintiff's property in North Dakota at $78,850,024.00." Here is an express admission that the assessment was in part at least based "upon this evidence" (the mileage factors) and yet the Circuit Court of Appeals says that "there is no evidence as to how the Board reached its results" and that "appellant has failed to establish that the Board was guided by or was largely influenced by the use of any particular method".

The state's valuation of $63,307,629.00 in Exhibit P which was itself $15,500,000 less than the assessment, as well as all of the other valuations in that exhibit, was based upon the use of five year figures and various mileage prorates. If we are to assume with the Circuit Court of Appeals that neither the assessment nor the valuation upon which it was based were guided or influenced by mileage prorates, we must, if we are to be consistent, eliminate mileage prorates from Mr. Baker's computations of value which were offered to justify the assessment.

If these mileage prorates are eliminated, we are left with his system value of $345,188,820.00 for 1933 and with the fact that less than 1/7 of the plant is located in North Dakota. This would indicate a North Dakota value (based upon pre-depression earnings and stock and bond prices) of only $49,000,000 and would leave some $30,000,000 of the assessment entirely without any pretense of justification, instead of only $15,000,000. It is only by using the mileage prorates that Mr. Baker obtains a computed value as high as $63,000,000 and that he reduces the arbitrary addition to as little as $15,000.000. If the Circuit Court of Appeals is right and if we are to assume that mileage prorates had nothing to do with the matter, then the state is left with the burden of explaining an arbitrary excess of $30,000,000 above any amount that the state could compute, even on the basis of pre-depression prices, without the use of mileage prorates.

We submit that a court of equity should not divorce itself from the ordinary processes of common sense and should not bow down and worship at the shrine of empty and misleading technicalities. We submit that no reasonable man in the exercise of ordinary common sense can doubt, after reading paragraph G of the Answer, and the other evidence referred to above, that the 1932 assessment was not only guided and largely influenced by the five year figures and the mileage prorates but that it was entirely controlled by them, and could not have been determined in any other way. To hold that this has not been sufficiently proven because we did not negative the possibility that there may have been some other lawful computations before the Board, when the state's own witness confesses that after diligent search extending over several months he has been unable to discover any, and when it clearly appears that there

are no possible lawful computations by which such a result could be reached, is to carry the refinements and technicalities of reasoning to an extent that would have shamed the mediaeval schoolmen.

We have gone into this question at greater length than it deserves because it is the sole basis for the adverse decision of the Circuit Court of Appeals. Feeling confident that this court will reach the conclusion that the use of the five year figures and the mileage prorates is not only proven but admitted, we proceed to discuss the effects of this method of computation in crediting North Dakota with values which had ceased to exist, and with values of properties actually located outside the state.

B.

In basing the assessment upon earnings and stock and bond prices of 1927 to 1931, the Board was in effect assessing values of an obsolete period which were no longer in existence in 1933.

We have seen that the 1932 assessment, which was adopted for 1933, was based upon earnings and stock and bond prices for the years 1927 to 1931. The earnings for these five years and for the following year 1932 were as follows (Ex. D, R. 255):

1927	$29,202,540
1928	31,294,069
1929	32,457,523
1930	21,912,508
1931	12,669,420
1932	1,290,551

It will be noted that in 1932, the last year immediately preceding the 1933 assessment, which is now in issue, the system earnings had fallen to $1,290,551, or about 5% of the 1929 earnings. The 1932 assessment was made in September, 1932, before the amount of the 1932 earnings was known, and therefore, of course, no effect was given to these shrunken 1932 earnings in the 1932 assessment. And when the same assessment was adopted a year later for 1933, it follows that while the low 1932 earnings had then become known, no effect was given to them and the dominating figures in the valuation continued to be those of the years 1927 to 1931 (1927 being six years before the 1933 assessment).

The total corporate stock and bond prices (of which 30.29% represented non-operating assets not forming a part of the railroad system, Ex. I, R. 265) for the years 1927 to 1932 were as follows (Ex. B, R. 251):

1927	$590,508,029
1928	606,649,827
1929	609,626,431
1930	571,294,190
1931	461,845,051
1932	296,301,177

It will be noted that the total sytem stock and bond prices (including non-operating assets) had fallen from $606,000,000 in 1929 to $296,000,000 in 1932 or less than half. But the 1932 figure was not considered in making the 1932 assessment. Exhibit G of the Answer quoted above shows that the figures which were used were those of the years 1927 to 1931. And since no effect was given to this reduced value in the 1932 assessment, it follows that no effect was given to it in 1933 when the same assessment was adopted, although by that time the

1932 figures were complete and were well known. The 1933 assessment was, therefore, in effect based upon stock and bond prices of the years 1927 to 1931, ignoring the greatly shrunken values of 1932.

The average of the earnings for the five years 1927 to 1931 was $25,507,192.00. The average of the earnings for the three years 1930 to 1932, immediately preceding the 1933 assessment was $11,950,826.00. In other words, the 1932 assessment (and therefore the 1933 assessment which was in the same amount) was based upon the earnings average of a five year period commencing six years before the 1933 assessment and omitting the immediately preceding year, and which was more than double the average of the three years immediately preceding the assessment and twenty times that of the single year immediately preceding. This indicates the excessive and dominating weight given to the boom period earnings of 1927, 1928 and 1929 in fixing an assessment for 1933, and the complete ignoring of the shrunken depression earnings.

The average of the stock and bond prices for the years 1927 to 1931 was $567,984,705.00 and the peak figure was the 1929 price of $609,626,431.00, while the price had fallen in 1932 to $296,301,177.00, of which only 68.71% represented railroad value. The later figure, as pointed out above, was given no weight in the 1932 assessment and, therefore, none in the 1933 assessment (although by that time it was well known) while dominating effect was given to the boom prices of 1927, 1928 and 1929.

An appraiser valuing securities for probate or other purposes and finding them actually selling currently at $20 a share in 1933, would scarcely be permitted to appraise them during that year at $60 a share, merely because they had sold six years before at $100 a share, or because $60 was a five year

average. He would not be permitted to value securities far above their actual current buying and selling price merely because in past years they had had a higher value which no longer existed. And yet in this case the taxing authorities acted even more irrationally than this, because they gave no weight whatever to current figures, either for 1933 or 1932, and gave dominating weight to the large figures which had existed four, five and six years before the date of the assessment.

It is admitted in paragraph L of the state's Answer (R. 31, 32), that if independent computations had been made for 1933, by the methods used in 1932 and described in paragraph G of the Answer (except that these methods would be applied to the reduced figures for the five years ending in 1932 instead of to the five years ending in 1931), the computed value for 1933 would have been reduced by approximately $13,000,000, and in spite of this no reduction whatever was made in the 1933 assessment.

Petitioner's gross revenues had fallen from $126,000,000 in 1928 and 1929 to $55,000,000 in 1932. The traffic had fallen from 10,000,000,000 revenue net ton miles in 1928 and 1929 to 4,000,000,000 in 1932 (R. 65). A careful and thorough analysis of Great Northern traffic commodity by commodity, and of permanent changes which had taken place in transportation conditions, indicated that this shrinkage was due only in part to the depression and that about half of it was due to permanent changes in traffic conditions which would persist even after the end of the depression and after a resumption of normal general business conditions throughout the country. The permanent changes resulted from diversion of traffic to the Panama Canal, highway vehicles, pipe lines, aeroplanes, etc., to various changes in commercial and agricultural methods which tended to shorten railroad hauls, and to very drastic rate reductions which were due in part to action by the Inter-

state Commerce Commission and in part to voluntary action by the carrier taken in an effort to hold its remaining traffic against further diversions to competing forms of transportation. This analysis appears on pages 65 to 70 of the record and concludes with an estimate that half of the shrinkage since 1929 is permanent and that the company could not reasonably hope for gross revenues in excess of $86,000,000, even after the end of the depression.

Based upon this amount of gross revenue, the General Auditor of the company made a careful analysis of permanent changes which had occurred in operating expenses and estimated that the company could not reasonably expect to earn a net railway operating income of over $14,000,000, even after a return of normal general business conditions (R. 121, 122).

The permanence of this shrinkage in railroad earnings and the fact that new conditions had caused drastic changes in transportation conditions and drastic reductions in railroad earnings is recognized in a report of the Committee on Interstate and Foreign Commerce of the House of Representatives, 74th Congress, First Session, Report No. 1560 recommending passage of H. R. 3263, a copy of which is attached to this brief as Appendix "C".

From the fact that the actual earnings for the three years preceding the assessment averaged only $11,950,826.00, and the fact that there was no prospect of increasing these in the future above $14,000,000, it follows that a valuation based upon average earnings of $25,507,192.00 (the average for the five years preceding the 1932 assessment) clearly resulted in an assessment which was levied against values which may have existed in the pre-depression boom years, but which had permanently disappeared and which no longer existed in the year 1933.

That a failure to give adequate recognition to changed economic conditions is not within the permissible discretion of an administrative tribunal and that the court will take judicial notice of the present depression, is the effect of the decision in *A. T. & S. F. Ry. Co. v. United States*, 284 U. S. 248, 52 S. Ct. 146. At page 260 this court said:

> "There can be no question as to the change in conditions upon which the new hearing was asked. Of that change we may take judicial notice. It is the outstanding contemporary fact, dominating thought and action throughout the country. As the Interstate Commerce Commission said in its recent report to the Congress, 'a depression such as the country is now passing through is a new experience to the present generation'. The Commission also recognized in that report 'the very large reductions in railroad earnings which have accompanied the economic depression', and stated that 'the chief cause of these reductions has been loss of traffic'. For 'in such depressions the railroads suffer severely. Their traffic is a barometer of general business conditions'."

Referring to suggestions regarding the wide discretion of the Commission, the court said on pages 261 and 262:

> "These suggestions would be appropriate in relation to ordinary applications for rehearing, but are without force when overruling economic forces have made the record before the Commission irresponsive to present conditions."

The following language on page 262 seems equally applicable to a tax board:

> "We are thus brought to the fundamental considerations governing the authority of the Commission. It has broad powers and a wide extent of administrative discretion, with the exercise of which, upon evidence, and within its statutory limits, the courts do not interfere. The important and salutary functions of the Commission to

enforce public rights are not to be denied or impaired. But the Commission, exercising a delegated regulatory authority which does not have the freedom of ownership, operates in a field limited by constitutional rights and legislative requirements."

Following this the court held that failure to recognize changed economic conditions "was not within the permitted range of the Commission's discretion."

It would seem to follow that an assessment for 1933 which can only be justified by ignoring depression conditions and going back to the boom years of 1927 to 1929 is not within the permitted discretion of a Tax Board.

In the case of *In re Assessment of Kansas City Southern Ry. Co.*, 168 Okla. 495, 33 P. (2d) 772, the court held that an assessment for 1933 based upon earnings and stock and bond prices for the five years immediately preceding the assessment were so arbitrary that it must be cancelled, upon the ground that the five year period included boom year earnings of an obsolete economic era which no longer afforded a logical measure of probable future earnings. The court said (p. 786, Pac. Rep.):

"The court takes judicial knowledge that there has been an era of depression, nation and world wide. This has had its destructive influences on railroad property as well as other property.

* * * * * *

"We do not think it tenable that those two years, 1928 and 1929, should be used in reflecting an assessed valuation of the railway property in 1933.

* * * * * * *

"We have been passing through an entirely different economic and industrial era since the years 1928 and 1929. Panicky conditions have prevailed. The organic condi-

tion of the railroad, its ties, rails, equipment, etc., are perhaps substantially the same, usual wear and tear excepted, but the figures conclusively prove that there has been a loss of earning power occasioned by other competing transport agencies, bus lines, truck lines, and air lines. The railway company asserts with confidence that this loss of business will not return to the railway company.

In the light of these facts, we are of the opinion that the taxable value of the railway company as of February 1, 1933, cannot be determined by measuring the peak of prosperity in the years 1928 and 1929 with the income derived during the commercial disaster of the business, in the years 1930, 1931 and 1932, and that the years 1930, 1931 and 1932 constitute a measurably substantial period of time for the purpose of sufficiently reflecting the proper assessable value of the property in question fixed as of February 1, 1933."

Our case is stronger than the Kansas City Southern case because there the Board had actually attempted to exercise its functions in 1933 and had based its computation upon the five preceding years including 1932 while here the assessment can only be computed by eliminating 1932 entirely and going back as far as six years before the assessment.

It is clearly established therefore, not only by the facts and by sound common sense reasoning but also by the decisions, that a large part of the very apparent excess in the assessment now at issue was levied against values of an obsolete period and against values which no longer existed in 1933.

We next proceed to show that another large part of the assessment was levied against property actually located outside the state.

Of the total amount of the assessment, approximately $20,000,000 was levied against properties outside the state and beyond its jurisdiction.

1. *The North Dakota trackage consists largely of relatively cheap branch lines. The more valuable terminals and more costly mountain construction are located outside the state.*

By far the largest terminals on the Great Northern Railway are at the eastern and western ends of the system, in the Twin Cities and on Lake Superior in the east and on Puget Sound in the west. The estimated cost of reproduction less depreciation of these three terminals alone was $68,804,121 (Ex. 4, R. 75, 76, 230). The total figure for the entire system in the United States is $532,538,184 (Ex. 7, R. 232) so that these three terminals comprise about 13% of the total physical property of the system. On the other hand, these terminals include only 53 miles of road (R. 76) out of a total of 7,591 miles (Ex. 6, R. 231). In other words, 13% of the property is included in less than 1/10 of 1% of the mileage at the extreme eastern and western ends. The cost per mile of road in the terminals is about $1,300,000 as compared with $40,779.00 for North Dakota (Ex. 7, R. 232). Another way of stating it is that one mile in these terminals contains as much physical plant as 32 average miles in North Dakota.

The total cost of reproduction less depreciation of the property in North Dakota is $78,190,762 and the mileage is 1917.41 (Ex. 7, R. 232). In other words, the 53 miles in these three terminals contain almost as much physical plant as 1917 miles in North Dakota.

In *Fargo v. Hart*, 193 U. S. 490, 24 S. Ct. 498, the court in attempting to state a very extreme hypothetical case said:

> "But it is recognized in the cases that if, for instance, a railroad company had terminals in one state equal in value to all the rest of the line through another, the latter state could not make use of the unity of the road to equalize the value of every mile."

Here we have a specific case falling almost exactly within this statement.

In addition to these three large terminals, there are other smaller terminals located both in and out of North Dakota as listed on Exhibit 5 (R. 230). But the larger of these smaller terminals are located outside of North Dakota, and there are more of them in proportion to mileage outside the state than inside (R. 76).

Disregarding the terminals and considering only the road itself, the miles in North Dakota are not equal to those on the balance of the system. In North Dakota there are 735 miles of main line and 1183 miles of branches. 61.7% of the total consists of branches, and the branh mileage is 161% of the main track mileage, while on the balance of the system only 43.5% is branch line mileage (Ex. 6, R. 231, 74, 75). On these branches the traffic is light and it is not necessary to provide so much construction for reducing grades and curves (R. 75).

North Dakota is a relatively level prairie state of simple railroad construction and without large terminals or shops (Complaint paragraph XII, R. 9; Answer, Part II, paragraph I, R. 28). The average mile in North Dakota contains very much less of all the units of construction making up the railroad than an average mile outside. It has only 80.5% as much steel rail per mile, 59.5% as much grading, less than 56% as much bridging, 63.9% as much signal apparatus and no snowsheds (Ex. 3, R. 229, 75). There are fewer stations and fewer division terminals in proportion to miles of road in North Dakota than there are on the balance of the system (R. 75).

As a result of all of these conditions, the average mile outside North Dakota contains $80,076 worth of construction and physical property as compared with $40,779 in North Dakota, or nearly twice the amount (Ex. 7, R. 232, 77). In other words an average mile of property outside the state is the same in length but greater in depth and breadth, size of rail, number of sidetracks and accessorial structures.

If we had built the entire 7500 miles of line with the same amount of grading, rail, etc., which was used in North Dakota and at the same cost of $40,000 per mile, the total system cost would have been approximately $300,000,000 instead of $564,000,000 (Ex. 7, R. 232). A mileage prorate to North Dakota might then be fair. But in addition to this, we have added an additional $264,000,000 of plant to the property lying entirely outside the state of North Dakota. It is when the mileage prorate is applied to this additional $264,000,000 that our protest arises.

Not only does the average mile in North Dakota contain less physical property, but it also originates less traffic, and carries, less traffic than the average mile outside, and is, therefore, less valuable from the standpoint of earnings. Exhibit 13 (R. 241) shows that North Dakota originates from 645 to 1204 tons per mile in different years as compared with from 990 to 3689 tons for the outside miles (R. 104, 105). Exhibit 14 (R. 241) shows that North Dakota trackage carries from 474,000 to 827,000 tons per mile as compared with from 528,000 to 1,111,000 tons outside (R. 105).

The physical situation is well summarized by this court in *Wallace v. Hines*, 253 U. S. 66, at 69, 40 S. Ct. 435, where the court said:

> "As the law is administered, the tax commissioner fixes the value of the total property of each railroad by the total

value of its stocks and bonds and assesses the proportion of this value that the main track mileage in North Dakota bears to the main track of the whole line. But on the allegations of the bill, which is all that we have before us, the circumstances are such as to make that mode of assessment indefensible. North Dakota is a State of plains, very different from the other states, and the cost of the roads there was much less than it was in mountainous regions that the roads had to traverse. The state is mainly agricultural. Its markets are outside its boundaries and most of the distributing centers from which it purchases also are outside. It naturally follows that the great and very valuable terminals of the roads are in other states. So looking only to the physical track the injustice of assuming the value to be evenly distributed according to main track mileage is plain."

2. *The outside terminals and costly mountain construction, while concentrated in short mileage contribute as much to transportation service and to system value in proportion to cost and volume of plant as do the cheaper portions of the road where the same investment is spread over more miles.*

It is obvious that a railroad could not exist and function without terminals. It is in the terminals that separate cars are combined into large trains so that freight can be moved over the road in large volume, and it is through the destination terminals that the large trains are broken up and delivery effected. Without terminals, cars would have to be moved as they might come upon the road in trains of from one to half a dozen cars and at greatly increased cost and at much higher rates. It is perfectly apparent that the terminals play as large a part in effecting the transportation between consignor and consignee as do the transcontinental tracks.

The same thing is true of mountain tunnels. By piercing a mountain with a single mile of tunnel costing a million dollars, we may avoid building a hundred miles of roundabout line at an even greater cost. The single mile of tunnel may contribute as much to the efficiency of transportation as a hundred miles of roundabout trackage. Transportation involves not only the overcoming of space resistance but also all other natural obstacles such as rivers and mountains. Plant which is required to bridge rivers, pierce mountains or elevate traffic over a mountain range contributes as much to the final result as does the trackage which is laid across a level prairie and which overcomes nothing but space.

It follows that a million dollars invested in a single mile of terminals or in a single mile of bridge or tunnel is as much entitled to a return upon every dollar of the investment, as is a million dollars which is spread out over 100 miles of prairie line. If this were not so, no investor could be found who would provide the funds for construction of the more costly parts of the line. The fact that a million dollars worth of investment is spread over more miles in one state than in another is no indication that it contributes more to the total transportation result or that it is entitled to a larger share of the system value.

About 1/3 of all operating costs are incurred in terminals (R. 117). As measured by cost, therefore, about 1/3 of the total transportation effort is expended in the terminals and 1/3 of the total transportation service is performed there. This would indicate that the use value of the terminals, based on the actual service they perform is a very substantial part of the total use value or commercial value of the system.

It is true that the system may not earn an adequate return upon its entire cost and its commercial value may be far below

its reproduction cost. The commercial value of the Great Northern system today amounts to hardly more than one-third of its reproduction cost. But however small the return may be, the money which is invested in tunnels and terminals is entitled to share in that return dollar for dollar with the money which may be spread out over more miles of cheap line in North Dakota.

It is also obvious that whatever value the terminals and costly mountain construction may have is included in the total system value of the property, when that system value is computed upon the basis of earnings or stock and bond prices. The stock and bond prices depend upon the earnings and the earnings are the joint product of all portions of the line and all of the service. They are the result of the terminal and mountain operations as much as they are of the ordinary line trackage. Therefore, when we apportion system value between states, whatever the basis of apportionment may be, we are apportioning a value which includes the value of the terminals as well as that of the miles of road, and we must see to it that the method of apportionment credits back the terminal portion of the system value to the state where they belong and that it does not spread them over intermediate states. These propositions are axiomatic but they are lost sight of in the arguments which are advanced in favor of the mileage prorates of system value and it is, therefore, important that we have them in mind before discussing the effects of the mileage prorates.

With these elementary principles in mind, we proceed to consider the question as to where these terminal values can lawfully be assessed.

3. *The right to assess and tax each portion of a railway system belongs solely to the state where that portion is located.*

This proposition presents an issue which has been in bitter dispute between the prairie states and the terminal states for many years. The terminal states contend for the right to assess and tax the value of the terminals located within their borders while the intermediate prairie states contend that the terminal values should be spread equally over the line and that they should share in the assessment.

The argument for spreading the terminal values is that the road is a unit; that the terminals are provided to serve miles of road in the prairie states as much as to serve the miles in the terminal states; and that it is the intermediate road miles which give the terminals their value and that without the intermediate road miles, the terminals would have no value.

It is equally true that the intermediate road miles would have no value without the terminals and that it is, therefore, the terminals which give the road miles their value. It would be equally sound to conclude that some portion of the road mile values should be taken away from the prairie states and credited to the terminal states.

The fact is, of course, that either portion without the other would have nothing but scrap value. It is the combining of the two that raises the value of each from a scrap value to a cost or use value. In this sense, it is true that it is the road miles which create the use value in the terminals, but it is also true that it is the terminals which create the use value in the road miles. We might go farther and say that every single mile of road creates the use value in all of the other miles, for if a single mile of road were permanently removed, the rest of the road would be useless.

But when the road miles in the prairie states are credited with the full use value which results from their combination with the terminals, the prairie states have been fully credited

with all of the value that they are entitled to as a result of their connection with the terminals. We cannot go further and credit them in addition with some portion of the use value of the terminals, any more than we can credit the terminals, in addition to their own full use value, with some portion of the use value of the road miles. It would be equally sensible to argue that each mile of road, in addition to its own full use value, should be credited with some portion of the use value of all the other miles, because without it the other miles would be useless. To credit one portion of the railroad with a part of the use value of another portion would be to leave the latter portion without its full use value, and this would be contrary to the fundamental principles expressed above.

Taxes are levied against property to pay for the exercise of the functions of government in the state where the property is located. The state where terminals are located provides the police and fire protection for the terminal property. It also provides for highway access, education of the children of terminal employes and of all other governmental functions. The intermediate states provide none of these things and incur no governmental expenses because of the terminal property. It is a universal rule that property should be taxed where located, and there is not the slightest reason for any exception in the case of railroad terminal property.

However, an abstract discussion of the underlying principles seems unnecessary, because it is so firmly established by the decisions of this court that terminal values can be assessed only in the states where the terminals are located and that they cannot be assessed in part by the intermediate states.

In *Fargo v. Hart*, 193 U. S. 490, 24 S. Ct. 498, this court said:

> "It is obvious, however, that this notion of organic unity may be made a means of unlawfully taxing the privilege,

or property outside the state, under the name of enhanced value or good will, if it is not closely confined to its true meaning. So long as it fairly may be assumed that the different parts of a line are about equal in value, a division by mileage is justifiable. But it is recognized in the cases that if, for instance, a railroad company had terminals in one state equal in value to all the rest of the line through another, the latter state could not make use of the unity of the road to equalize the value of every mile. That would be taxing property outside of the state under a pretense."

In *Wallace v. Hines*, 253 U. S. 66 at 69, 40 S. Ct. 435, the court said:

"As the law is administered, the tax Commissioner fixes the value of the total property of each railroad by the total value of its stocks and bonds and assesses the proportion of this value that the main track mileage in North Dakota bears to the main track of the whole line. But on the allegations of the bill, which is all that we have before us, the circumstances are such as to make that mode of assessment indefensible. North Dakota is a State of plains, very different from the other states, and the cost of the roads there was much less than it was in mountainous regions that the roads had to traverse. The state is mainly agricultural. Its markets are outside its boundaries and most of the distributing centers from which it purchases also are outside. It naturally follows that the great and very valuable terminals of the roads are in other states. So looking only to the physical track the injustice of assuming the value to be evenly distributed according to main track mileage is plain."

In the recent case of *Rowley v. C. & N. W. Ry. Co.*, 293 U. S. 102, 55 S. Ct. 55, the court said:

"Where, as in this case, the evidence requires a finding that the railroad in one of the states reached by the system is clearly shown to be worth much less than the aver-

age value per mile of the system, an apportionment on mileage necessarily assigns an excessive amount to that state, and the use of that basis as the sole measure for apportionment must be condemned as arbitrary."

See also *Pittsburgh, C. C. & St. L. Ry. Co. v. Backus*, 154 U. S. 421, 14 S. Ct. 1114; *Union Tank Line Co. v. Wright*, 249 U. S. 275, 39 S. Ct. 276; *Southern Ry. Co. v. Kentucky*, 274 U. S. 76, 47 S. Ct. 542.

In these cases, the apportionment had been attempted upon the basis of miles of road only and not upon a combination of several factors, but they establish the proposition very definitely that the power of assessing and taxing terminals belongs exclusively to the states where the terminals are located and that the terminal values cannot be spread for purposes of assessment over the intermediate states, and that any method of apportioning system value which accomplishes that result is necessarily unlawful.

In the case now at bar the attempted apportionment was based upon a composite of five different factors, and it remains to consider only whether the unlawful spreading of terminal and other out-state values is avoided by the composite factors used by the State of North Dakota.

4. *The factors used in the North Dakota computations unlawfully credit to North Dakota values of terminals and mountain construction actually located in other states.*

We have already quoted paragraph G of the Answer in which the state admits that the computations upon which the 1932 assessment was based were made by apportioning the value of the entire railroad system to North Dakota by certain allocation factors. The five factors as enumerated in paragraph IX of the Complaint upon which the first computation

is based were as shown in the following list which also shows the ratio of each for North Dakota for 1932 as taken from Exhibit N.

1.	Miles of all track	20.19%
2.	Physical property	13.84%
3.	Car and locomotive miles	19.90%
4.	Ton and passenger miles	18.65%
5.	Gross earnings	18.45%

Paragraph G of the Answer states that one computation was made by the use of all five of these factors, another by the use of factors 3, 4 and 5 and still a third by the use of factors 1, 3, 4 and 5.

The number of cars moved one mile and engines moved one mile in and out of North Dakota is computed by measuring the mileage moved between the stations of origin and destination and does not include any movement in switching service in the terminals. Similarly the number of tons moved one mile and passengers moved one mile includes only the movement between the stations of origin and destination and does not include any switching movements (R. 78, 115).

In other words, these factors are dependent entirely upon miles of road over which the shipment moves and they are not affected in any way by the location of terminals. A state containing terminals is not for that reason credited with any more of these miles of movement over the road, and a state without terminals is not for that reason credited with any less.

The gross revenues credited to North Dakota include all earnings wholly within the state and a portion of through earnings on shipments moving in any part within the state, equal to the proportion which the miles of movement on that shipment in North Dakota bear to the total miles of movement of that

particular shipment. Here again the apportionment is made upon the basis of miles of road over which the shipment moves and is in no wise affected by the fact that there may be terminals in one of the states and no terminals in another (R. 115). 92% of all of the gross revenues credited to North Dakota consist of a mileage prorate of through revenue, as the traffic in and through that state is almost wholly interstate (Complaint Par. VIII, Answer Par. E).

The gross revenue ratio on each shipment is therefore necessarily identical with the ton mile, road mile or track mile ratio on that particular shipment. The combined ton mile and passenger mile ratio for North Dakota for the five years ending in 1932 was 18.65% while the gross revenue factor is 18.45%. The two would, of course, be identical if rates were the same in and out of the state, and the gross revenue factor for North Dakota is slightly less only because the average revenue per ton mile and passenger mile on business which moves partly in North Dakota is slightly less than the average on traffic which does not touch North Dakota.

It is apparent, therefore, that the proportion of car and engine miles, ton and passenger miles and gross revenue in any state depends entirely on the miles of road in and out of that state over which the traffic moves, and that it does not depend at all on the location of terminals. As between two states of equal road mileage and equal traffic density these factors would apportion the system value 50-50. The fact that there might be valuable terminals in one state and none in the other would not affect any one of these ratios. If the terminals were originally in state A, the ratio would be 50-50, and if they were later removed out of state A and into state B, the ratio would still remain 50-50, and the system value including terminal values would still be apportioned equally. In other

words, these factors spread the entire system value, including whatever terminal values it may contain, equally over all miles of haul, and regardless of the location of terminals in one state or the other.

This would appear still more plainly if the line of road were all located in state A, with the shops and terminals located just across the boundary in state B. Here 100% of the car and engine miles, ton and passenger miles and gross revenue (the miles of haul factors) would be credited to state A and nothing to state B. If these three factors were used alone, the entire system value, including whatever value the terminals and shops in state B might have, would be assessed and taxed in state A, and state B, which actually contained the terminal and shop properties, would have nothing to tax.

We can again vary the case by moving the state boundary a little further from the terminals and leaving 10% of the road mileage in state B. This state would now be credited with 10% of the system value including only 10% of the terminals which are located 100% within her borders. Again, if the state boundary were at the center of the line, state B would then be permitted to tax 50% of her own terminals and state A would be credited with the other 50%. In other words, the right to tax the terminal values would depend not upon the location of the terminals but upon the location of the road miles. The state with the terminals would get no more than its road haul proportion of the system value and the state without terminals would get no less, and we could transfer the terminals from one state to the other without affecting the apportionment of value.

The theory underlying the use of the "miles of haul" factors seems to be that, while the track mile factor reflects nothing but the proportion of trackage in a state, the three miles of

haul factors reflect varying amounts of traffic density and, therefore, tend to correct the errors in the miles of track factors when used alone.

It is true that these three "miles of haul" factors reflect differences in traffic density as well as miles of road haul, and if one of the states had twice as much traffic density as the other, on the same road mileage, its miles of haul ratio would be twice as great. In other words, these ratios are not necessarily the same as the ratio of miles of road, since they are affected by varying traffic. But it would still be true that an apportionment made on these three factors would be without regard to the actual location of the terminals. With equal road mileage in two states, the density might be twice as great in the state without terminals, in which case 2/3 of the system value including 2/3 of the terminal value would be allocated to that state. If the terminal state were the one with double the density, it would thereby be credited with 2/3 of the system value. But this would be in recognition of the greater traffic density and greater earning power of its miles of road, and not in recognition of the location of its terminals. And whatever the difference in traffic density might be, the terminals could still be transferred from one state to the other without affecting the apportionment of value between them in the slightest. The point that we are making is that by this method of allocation, the state containing the terminals is not credited with their entire value but that on the contrary the terminal values are spread equally over all states either in proportion to track miles or miles of haul.

Because of its lighter traffic density, North Dakota's three "miles of haul" ratios are slightly less than its track mile ratio and, therefore, the composite five factor ratio credits North Dakota with slightly less of the terminal values than

would the track mile ratio if used alone. But this slight reduction gives no sufficient recognition to the smaller property value and density of the North Dakota road miles as compared with the larger property value and density of the miles of road outside, and it does not even tend to restore any terminal values whatever to the states where they belong.

It is true that the track mile factor is based upon miles of all track including side and yard track, instead of upon miles of road or miles of main line only. This factor includes all of the yard tracks in the terminals and so gives some slight extra credit to the terminal states. But it also counts every mile of cheap branch line in North Dakota and treats each as being equal to a mile of main line or to a million dollar mile in the Cascade Tunnel, across the Columbia river bridge, or in the large city terminals. The Great Northern line in North Dakota is a veritable gridiron of these cheaply built branch lines as shown on the map (Ex. 1, R. 227). The proportion of branch lines to main lines is 161% in North Dakota and only 76% on the balance of the system (Ex. 6. R, 231). The proportion is more than twice as great in North Dakota. As a result of treating each of these cheap branch lines as being equal to any other mile on the system, the "miles of track" factor, while it gives some slight credit to the terminal states for the yard tracks, gives even more credit to North Dakota for its cheap branches and the net effect is that the miles of track ratio for North Dakota is the highest of the five factors used. It was 20.19% in 1932 as compared with the five factor average of 18.20%. The total miles of all track in the three large terminals, including all yard tracks, is only 537 miles, of which 53 miles are main line, leaving 484 miles of side track (R. 76, 86). Any credit to the terminal states for these, is more than offset by the fact that there are 1,183 miles of

branch lines in North Dakota which are given undue credit by the track mile ratio (Ex. 6, R. 231). It follows that this factor, instead of restoring terminal values to the terminal states, abstracts still more of them because of the large branch line mileage in North Dakota.

And even if the North Dakota branch lines did not afford this offset, the crediting of only 484 miles of yard tracks to the terminals (we ignore whatever offset there may be on account of yard and side tracks in North Dakota) is only about 6% of the 7591 miles of road on the system (Ex. 6, R. 231). And when this track mile factor is averaged with several others which give no credit for yard tracks in terminals, this 6% is thereby diluted and reduced to 1 or 2%. As 13% of the total plant is in the three terminals, and as 1/3 of the total operating expense is incurred in terminals, this small credit of 1 or 2% to the terminal states is totally inadequate.

It appears therefore that 4 of the 5 factors used by the state, viz., track miles, car and engine miles, ton and passenger miles, and gross revenue, all tend to spread the terminal values and credit them unduly to North Dakota. The fifth of the five factors used by the state is the physical property ratio, and as this is based on reproduction cost less depreciation, it alone gives full credit to the terminal states for their terminal properties. However, this is only one of the five factors used and has only 1/5 weight in the result. And the entire five factors were used in only one of the three computations in 1932, referred to in paragraph G of the Answer. In the other two computations, the physical property ratio was omitted. Five factors were used in one computation, four in the second and three in the third. In other words, the three road mile factors were each used three times, the track mile factor was used twice and the physical property factor was

used only once, making a total of 12 factors. It follows that in the final result the physical property ratio was given 1/12 weight and the mileage ratios were given 11/12 weight. The effect of using the physical property ratio in this way is, therefore, that instead of spreading the entire terminal values equally over miles of road or miles of haul, only 11/12 of the terminal values are so spread and 1/12 is credited to the state where the terminals are located.

Combining the physical property ratio of 13.84% with the other four raises the composite average to 18.20%. When the five factor apportionment is combined with that based upon four factors and three factors as described in paragraph G of the answer, the composite ratio is increased to 18.76% or 5% above the physical property ratio. And this 5%, applied to the 1932 system value of $415,278,961.00 as computed by the state (Ex. P. R. 277) (which is based largely upon boom period figures) credited North Dakota with more than $20,000,000 of outside values in the 1932 assessment which was adopted for 1933. In spite of the fact that the physical property ratio if used alone would give full credit to the terminal states, the fact remains that when it is combined with the other factors, and given a weight of only 1/12, its effect is so far lost that, even with this factor included, more than $20,000,000 of outside values are still credited to the state of North Dakota.

Our conclusion that the factors used by the state necessarily spread terminal values over intermediate states might be put into syllogistic form as follows:

(1) The terminals and mountain construction located outside North Dakota have an actual use value which is a part of and included in the system earnings and stock and bond value.

(2) The entire system value, including the terminal values is apportioned among the states.

(3) Not more than 1/12 of these terminal values is apportioned to the states where the terminals are located.

(4) It follows that 11/12 of the terminal values are necessarily spread over all states, regardless of location.

The defendants contend that the use of these mileage factors has been approved by this court in *Rowley v. C. & N. W. Ry. Co.*, 293 U. S. 102, 55 S. Ct. 55, and in other cases. It would be more accurate to say that assessments based upon mileage prorates have been before this court in cases where they were not condemned. It is not correct to say that they were approved because, while they were before the court, they were not in issue. There was no evidence in the Rowley case and no contention by the railroad that the apportionment based upon miles of haul did in fact credit any terminal values to Wyoming. That contention was made solely with reference to the miles of track factor. It was not pointed out to this court nor even claimed in that case that the miles of haul factors in themselves credited any terminal values to Wyoming, and indeed this may not have been the fact in that case. On the contrary, the sole contention was that the miles of track factor was the only one which wrongfully credited terminal values to Wyoming, and it seems to have been assumed by all parties that the miles of haul factors were sound in this respect. This court simply held that where the single miles of track factor, which would have been unlawful if used alone, was averaged with several other factors which were apparently conceded to be correct, the combination of the single wrongful factor with several other proper ones did not in itself defeat the assessment. In our case, however, it is an established and mathe-

matically demonstrable fact that four of the five factors necessarily credited North Dakota with terminal values, and that these four wrongful factors were used eleven times in the aggregate in determining the 1932 assessment, while the single lawful factor was used only once, and, therefore, given a weight of only 1/12 in the final result. It is demonstrated that the use of the four wrongful factors raised the composite average by 5% and credited North Dakota with more than $20,000,000 of outside values.

If by any stretch of interpretation the Rowley case can be regarded as affirmatively approving the use of mileage factors in the case of a railroad like the Great Northern and in the case of a state like North Dakota, and where the record contains a clear demonstration that these factors spread terminal values over the intermediate states, the decision should clearly be qualified or limited in its operation. If such a decision had been made upon such a record as this, it should clearly be reversed. We submit that this conclusion is undebatable.

5. *Some additional reasoning to the same effect.*

We believe that the foregoing arguments conclusively establish the proposition that the state's apportionment factors actually and unlawfully credit terminal values to North Dakota and that this proposition does not require any further support. However, there is a great deal of further support in the record, and we hesitate to leave this question without referring to it. If the court feels already convinced by the foregoing argument that terminal values have in fact been credited to North Dakota, the next six pages may be skipped. If any doubt upon this question still remains, we believe that the following arguments will settle it.

One way to consider the track mile and miles of haul ratios, is to consider the track mile ratio as an attempt at measuring the relative amount of property in North Dakota by miles of track, and the miles of haul ratio as being an attempt to measure the proportion of the total service or business of the company which is carried on in North Dakota by miles of haul. A mile of track is used as a measuring stick to measure the amount of physical plant inside and outside the state, and a mile of haul (whether of tons, passengers, cars or engines) is used as a measuring stick to measure the service performed inside and outside the state. But in using a mile of track as a measure of plant volume or property volume, we are using a measure that contains only half as much volume when used inside the state as when used outside the state. It indicates that there are 20% as many of these measures inside the state as there are on the system, but as the measures used inside the state are only half-size, the ratio is entirely misleading.

A similar result takes place when we use miles of haul to measure relative service, because this measuring stick measures nothing but road haul service and entirely fails to measure terminal service, amount of equipment repairs, amount of plant provided, etc.

We must remember that railroad service includes at least four elements: (1) providing the plant and equipment, (2) keeping it in repair, (3) performing the terminal service, and (4) moving the traffic over the rails. The three North Dakota factors showing miles of road movement reflect only the fourth element out of the total service, i. e., the road haul. But for every mile of movement *outside the state,* the company has to provide twice as much fixed plant on the average, and also to repair and maintain twice as much plant, as well

as performing a heavy terminal service. In this respect an average mile of movement outside the state represents more total service than an inside mile, and while the three "miles of haul" factors indicate that about 18% of the miles of haul are in North Dakota, this is no indication whatever that 18% of the total business is done there or 18% of the total money earned there, since the balance of the system, in addition to providing the other 72% of the miles of haul, also provides nearly all of the terminal and repair service and a proportionately larger part of the total plant.

An average car mile in switching service in the large terminals, which are located in other states, requires about 15 times as much effort and costs about 15 times as much in operating expenses as the average car mile on the road (R. 114-117). In using a car mile ratio, ten or fifteen cents worth of transportation service in North Dakota is assumed to be an equivalent unit with $3.00 worth of transportation service in the Minnesota and Washington terminals, simply because both are spread over a mile of ground (R. 114).

We have pointed out above that if the entire road mileage were located in one state, with the terminals, shops and general office buildings just across the boundary in another, the miles of haul ratios would allocate to the first state 100% of the entire property including the property located in the second state. We have an actual situation on the Great Northern Railway which is very close to this. Our line which carries iron ore from the Minnesota iron ranges to the Lake Superior docks is located 90 miles in Minnesota and ten miles in Wisconsin. However, the 10 miles in Wisconsin contain the yards, terminals, repair shops and docks, and the actual reproduction cost is about $16,000,000 in each state. So far as actual value of plant is concerned, the two states are equal. But

Minnesota has 90% of the total miles and of the miles of haul, and the five factor ratio including the physical property factor would be about 80%. With an aggregate value of $32,000,000, Minnesota, under the five factor formula, would assess her $16,000,000 plant at 80% of the total, or $25,600,000 and Wisconsin would assess her $16,000,000 plant at $6,400,000 (R. 96, 114, 139).

The situation as to the movement of North Dakota wheat to the Twin City and Lake Superior terminals is the same in principle and differs in fact only in that the state boundary is nearer to the center of the haul instead of close to the terminals (R. 140). In this situation, North Dakota and Minnesota each have 50% of the miles of haul and therefore, North Dakota instead of being credited with 90% of the terminal values is credited with only 50%. But in both cases, the terminal values are spread equally over the miles of haul without regard to the location of the terminals. These illustrations show the absurdity of apportioning system value according to track miles, or miles of haul, because thereby terminal values are abstracted from the state where they are located and credited to the states where the road haul is performed.

We also pointed out above that one mile of tunnel in one state might avoid the necessity for 100 roundabout miles of track, and that on every shipment, the car miles, ton miles, engine miles, etc., which would amount to 100 miles of haul if performed on a roundabout track, might be reduced to one if handled through a tunnel, merely because of the fact that the company had put its investment into a tunnel instead of into a roundabout track. Here again we have an actual illustration of this on the Great Northern. The towns of Skykomish and Leavenworth, Wash., separated by a mountain barrier, could have been connected by 150 miles of 1% grade over

the summit or by 50 miles of line using tunnels (R. 77). The company chose the latter alternative at great cost, and by the erection of a costly and valuable plant, thereby reducing from 150 to 50, the number of track miles, car and engine miles, ton and passenger miles and the mileage prorate of gross revenue between these two points in Washington. Because a more costly, more efficient and more valuable plant was built between Skykomish and Leavenworth, the amount of through revenue and the amount of system value allocated to this segment of line under the North Dakota formula are reduced to one-third. The better and more concentrated the railroad plant becomes the less it is worth. On the other hand, the value which is thus taken away from the improved part of the line is spread over the unimproved portions. The effect is to give to North Dakota and other states a correspondingly larger percentage of the total system track miles, operating miles and service miles and, therefore, of the system value.

Presumably the heavier tunnel investment reduced operating expenses and thus increased system net earnings and stock and bond values, so that under the North Dakota method, North Dakota and every other state would claim a higher percentage of a higher system value, and, therefore, several million dollars more value in North Dakota because of the creation of valuable property in Washington (R. 77, 117-118). Because Washington contained a more costly plant, North Dakota would be given a higher value and Washington a lower value than would be the case if we had constructed a cheaper plant in Washington or had chosen the alternative of constructing more miles of less usefulness and less value in Washington.

And after the original tunnel line had been completed between Skykomish and Leavenworth, Wash., the company built a still longer tunnel at a lower grade and made other line re-

visions at a cost of $26,000,000 which effected a further shortening of 18 miles of distance and presumably reduced operating expenses and increased the system value accordingly (R. 77). The effect of this improvement in Washington was to still further reduce the percent of all mileage factors in Washington and to correspondingly increase them all in North Dakota and other states, thus again giving to North Dakota under the state's formula a yet higher percentage of a still higher system value, and giving Washington a smaller percentage, not because of any improvement in North Dakota but because of the creation of additional plant in Washington. An assessment by North Dakota on this basis is clearly an assessment upon property in Washington and is clearly condemned in *Fargo v. Hart* and similar cases.

The objections which we have been making to the use of these miles of haul ratios are objections that would apply to any intermediate state. There are other weaknesses in the use of these ratios which apply particularly to North Dakota. For example, an average carloading in North Dakota is around 16 tons while the average carloading on the balance of the system is nearly 30 tons (R. 116, 130, 135). This is due to the large amount of less than carload tonnage moving in lightly loaded cars on North Dakota branch lines (R. 135).

While a locomotive on the iron ore carrying lines of the Great Northern in Minnesota hauls 170 cars or twelve or thirteen thousand tons per locomotive mile, a locomotive on the branch lines in North Dakota would haul about two to four hundred tons on the average. These particular engine miles in North Dakota have an actual value in volume of traffic handled equal to only 1/70 of those on the Minnesota ore lines (R. 116). The state's tax expert conceded that car and engine miles moving smaller tonnage should not be given as

much credit as car and engine miles with heavier tonnage (R. 201).

Exhibit 12, Schedule B, Line 7 (R. 239) shows that the movement of a thousand tons of freight one mile in North Dakota requires $7.19 worth of effort while the average movement of a thousand tons on the balance of the system requires $9.89 worth of effort. The ratio is nearly 10 to 7. This is, of course, because of the terminal and shop expenses in the other states. As the average carload in North Dakota is 16 tons and the average carload on the rest of the system is 30 tons, it is easy to compute that the movement of an average car one mile in North Dakota requires 11½¢ worth of effort while the movement of an average car one mile on the balance of the system requires 29.68¢ worth of effort.

Still another vice of all of the ratios reflecting miles of movement is that they ignore mileage made in switching service in the terminals and consider only the miles made in roadhaul between terminals (R. 78, 115). If there should be five or six miles of switching service after the car reaches a terminal, each of these miles costing as much as 15 roadhaul miles, the effect would be the same as if we excluded 75 to 90 miles of roadhaul service outside the state on each trip while including the entire mileage made in North Dakota.

We have seen that in computing gross revenues earned in North Dakota, interstate revenues are allocated in proportion to miles of road only (R. 87), and that 92% of all the traffic in North Dakota is interstate (R. 70). Approximately one-third of the service in an average through haul (as measured by cost) is performed in the terminals and two-thirds on the road (R. 117). The miles made in terminals are given no weight whatever in computing the gross revenue ratio, although they should be entitled to about fifteen times as much weight

as road miles (R. 79, 115). It follows that a prorate of interstate revenue in proportion to miles of road is virtually a repetition of the track mile ratio and accords an excess of credit to a state like North Dakota.

This concludes our argument upon this point. We submit that the spreading of terminal values over North Dakota is demonstrated:

(1) By the fact that the terminal values are included in the system value which is apportioned among the states and that since they are not credited to the terminal states, they must be spread over all states.

(2) By the fact that a track mile is a measuring stick of smaller volume when used in North Dakota than when used outside, and that miles of haul do not measure any part of the total railroad service except the haul over the road, and entirely fail to measure that part of the service consisting of the providing of the plant, the maintenance of plant and repair of equipment and the terminal service. As these are performed more largely outside the state, the three "miles of haul" factors necessarily spread them over all states in proportion to miles of road haul only, and thus give undue credit to North Dakota.

D.

Where the use of unlawful methods by the taxing officers has been shown, it is not incumbent upon the taxpayer to submit a proper method of computation or to prove the correct amount that is due.

In *Guy T. Helvering, Commissioner of Internal Revenue v. Walter W. Taylor,* No. 289, 293 U. S. 507, 55 S. Ct. 287, decided January 7, 1935, the court said:

> "We find nothing in the statutes, the rules of the board or our decisions that gives any support to the idea that

> the Commissioner's determination shown to be without rational foundation and excessive will be enforced unless the taxpayer proves he owes nothing or, if liable at all, shows the correct amount. While decisions of the lower courts may not be harmonious, our attention has not been called to any that persuasively supports the rule for which the Commissioner here contends.
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> * * * * * *
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> But, where as in this case the taxpayer's evidence shows the Commissioner's determination to be arbitrary and excessive it may not reasonably be held that he is bound to pay a tax that confessedly he does not owe. unless his evidence was sufficient also to establish the correct amount that lawfully might be charged against him."

Under this decision, it is not incumbent upon us to tell the state how to make its assessment. The state must itself find some method of valuing the property in North Dakota which will avoid crediting North Dakota with values outside the state. This might be accomplished by entirely avoiding the computation of a system value and by capitalizing the net earnings earned by the property in North Dakota alone. Or it might be accomplished by first computing a system value and then allocating proportionate part of that system value to the terminals and mountain construction outside the state, and deducting it from the system value before prorating the balance to North Dakota on the five factor formula. An apportionment of system value between the ordinary road mile trackage on the one hand and terminal properties and extraordinary mountain construction on the other might be made in proportion to cost. Any method that the state might see fit to adopt and that would be reasonable and used in good faith would be sufficient.

Or total system value might be apportioned between states in proportion to the physical property factor used alone. This

would appear to be defensible because it would allocate the system value in proportion to the volume in each state of the physical plant which produces the service and value.

It might be said in criticism of this that equal volumes of physical plant in different states might have different commercial values depending on traffic density, and that a million dollars worth of track in one state with a very heavy traffic density might be worth more than a million dollars worth of plant in another state with a very light traffic density. We submit, however, that the commercial or use value of equal investments in different portions of the line does not necessarily vary with traffic density.

It is a well-settled principle of rate-making that rates should be lower in regions of greater traffic density and higher in regions of less traffic density. This is necessarily so if railroads operating in low density areas are to be allowed to earn the same return on investment as railroads operating in high density areas. Relative values depend upon relative earnings and the earnings are a product of *the density times the rate.* A railroad or portion of a railroad with low traffic density should be allowed correspondingly higher rates. These rates should be so adjusted that the return upon every portion of the investment should be no more than is reasonable, and no less, and if single through rates are established for long hauls over different portions of the road with varying costs and varying densities, the through earnings should be credited to each portion in such a way as to yield the same relative rate of return upon each dollar of investment in all portions. If this were not so, investors would refuse to provide funds for the portions of the line where traffic is relatively light and costs high. We must bear in mind, therefore, that the relative value of different portions of the line depends upon earnings

and not upon density alone, because earnings are a product of density and rates.

Of course, there may be branch lines and other portions of a railroad system which cannot pay their operating expenses and which are a liability and not an asset and should, therefore, be credited with nothing but scrap value. However, these are exceptional cases, and we believe that prima facie at least, it would be difficult to attack an apportionment of system value based upon the physical property ratio alone, in spite of variations in traffic density in the different states.

If we were called upon to state what we believed to be the most scientific and accurate method of valuing the portion of a railroad located in any state, our suggestion would be that the net earnings in that state be determined and that the valuation be made either by capitalizing the net earnings or by apportioning the system value in the proportion that the net earnings in the state bore to those of the system.

Of course, before we can determine the net earnings in a state by deducting the expenses incurred in the state from the gross revenues earned there, we must determine what the gross revenues are. And in a state like North Dakota where 92% of the traffic is interstate, this requires an apportionment of through revenues between North Dakota and the balance of the system on some logical basis. We have seen that a road mileage prorate of such revenues is utterly valueless and unlawful because, while 1/3 of the service (as measured by cost) is performed in the terminals and, therefore, presumably something like 1/3 of the revenues are earned there, the mileage prorate spreads the entire revenue over the miles of road haul, and leaves nothing for the terminals. However, we believe that this difficulty can be met by apportioning the revenue from through interstate service in proportion to the cost of producing

the service. Where an interstate haul produces $100 in revenue, a state which incurs 25% of the cost of that haul would be credited with 25% of the revenue. Clearly, this is the basis upon which through revenues would be apportioned if the lines in each state were owned by independent connecting corporations.

Of course, the cost of producing the service should include the cost of providing the plant and repairing the equipment as well as the cost of moving the traffic. To determine the cost of providing the plant, we would determine the rate of return earned by the entire system, whether it were 2% or 10%; and apply that rate to the cost of the plant in each state. This total cost of providing the plant in each state, plus the total cost of operations (including terminal operations and all others) would then be divided by the ton miles moved in that state to determine the total cost per ton mile in each state for plant and operation. In this total cost would be included the cost of providing terminals, tunnels, bridges and other extraordinary structures as well as the cost of operating them, and an apportionment of through revenues in proportion to this cost, plus the revenues earned locally would be a scientific and accurate computation of the gross revenues earned in the state. A deduction of the expenses (which are easily computed) would give the net.

Exhibit 12 (R. 237-239) is a careful computation by this method which is fully described on pages 89 to 95 of the record. By this computation, North Dakota over a five year period produced 12.22% of the net earnings of the system and should, therefore, be credited with 12.22% of the system value instead of the 18.20% indicated by the five factor ratio.

The Circuit Court of Appeals made the curious mistake of assuming that our criticism of the assessment at issue was solely on the ground that the assessment was not computed

upon this net earnings basis, and that this was the only method which any state could lawfully use. The court says "The force of its (appellant's) attack upon that method (the five factor method) is based upon the argument that, in the situation here, the only approximately true method of allocation was one using the comparative 'expense of operation' in North Dakota and outside that state or upon the system". The court held that this method had not been presented to the Board and that it was new and untried, and, therefore, the assessment could not be set aside merely because it did not conform to this method.

Of course, this betrays a complete misunderstanding of our case by the Circuit Court of Appeals. Our attack upon the assessment (aside from the fact that it is levied against obsolete system values which no longer exist, and that $15,000,000 of it lacks any justification whatever) is based upon the fact that the mileage ratios assessed property outside the state. This is demonstrated to a mathematical certainty. Our case is complete there. It is based upon faults in the state's method, and not upon virtues of some other method. We do not have to prove what the proper method would be nor do we contend that the state is obliged to follow the best or most accurate method. Any reasonable method will do, so long as it does not assess outstate property. Exhibit 12 is offered as only one of several possible methods, and only for the purpose of showing that it is possible to make apportionments without violation of law. Failure to conform to the method suggested here is not at all the basis of our attack upon the mileage ratios and, because of this misunderstanding, if for no other reason, we submit that the decision of the Circuit Court of Appeals should be reversed.

We have proven the *fact* that values have been credited to North Dakota which belong in terminals outside the state,

and this has not been disputed in the evidence nor in the opinion by either court nor up to this time, in the briefs of the respondents. See for instance pages 20 and 21 of respondents' brief in opposition to petition for writ of certiorari where the whole question of the spreading of terminal values by the mileage factors is evaded. The entire argument of the respondents as well as the opinion of the Circuit Court of Appeals is based upon a denial that the Board ever used the mileage ratios, and we believe that we have effectively disposed of this question.

E.

Even assuming that no wrongful methods were shown and that there was no evidence whatever as to what methods were used, the facts that the assessment is treble the current value of the property and that the defendants confess their inability to justify it by any rational process are sufficient to prove arbitrary action.

Even if we forget that the 1933 assessment adopted that of 1932, and assume that the figure for 1933 was entirely independent of any previous assessment; even if we assume, as the Circuit Court of Appeals seems to hold, that there is no evidence that prices and earnings of a five year period were used and no evidence that system value was apportioned by the use of mileage prorates; and even if there were nothing in the case but the amount of the assessment of $78,832,888.00, the current earnings and stock and bond prices indicating an actual current commercial value of only twenty-five or thirty million dollars, and the confession of the defendants' expert witness that he could not find any evidence or method that would justify the assessment, and that the value computed by what the defendants claim to be the fairest method was only $63,307,629.00, we submit that on this evidence alone a court of equity should set aside the assessment.

The trial court found that there had been no over-assessment in 1932 or previous years, but refused to find whether or not there was any over-assessment for 1933 (Findings Nos. 8 and 10, R. 52, 53). The court found, however, that there was no evidence (other than the evidence of excessiveness) to show actual fraudulent intent or violation of legislative mandate (Finding No. 9, R. 52), and concluded that mere over-assessment, even though confessed to the extent above indicated, was not sufficient to show arbitrary action nor to warrant relief.

Judge Sanborn's concurring opinion in the Circuit Court of Appeals was as follows:

> "The power of the Federal Courts to enjoin the collection of State taxes upon the property of an interstate carrier has been so circumscribed, as pointed out by Judge Stone in his able opinion, that, although I have no doubt that the property of the appellant in North Dakota was over-valued for tax purposes in 1933, I concur in the conclusion reached in the opinion and the reasons assigned for it. I am not, however, in entire sympathy with the rule which seems to preclude any interference with such overassessments unless it clearly appears that they result from purely arbitrary action or from something akin to fraud. While death from an honest error of judgment may be preferable to death designedly caused, the effect upon the victim is the same. Overtaxation resulting from honest mistake or errors of judgment is as serious as that resulting from fraud, and constitutes just as unreasonable a burden upon interstate commerce. I regard state taxation of interstate carriers as a matter of national concern.
>
> In this case the defendants' own expert states that no method of computation with which he is familiar would produce a value for 1933 equal to that fixed by the State Board. To that extent we have a different situation here than in the Rowley case. That the value of the portion of appellant's system in North Dakota in 1933, after the ap-

pellant had been through three years of depression, even approximated the values of 1928 and 1929 is to my mind inconceivable. Possibly I am substituting my judgment for that of the Board, but the Supreme Court in Atchison, Topeka & Santa Fe Railway Co., et al. v. United States, et al., 284 U. S. 248, referred to a record made in a rate hearing in 1928 as pertaining to a 'different economic era', and said (page 262):

> 'This is not the usual case of possible fluctuating conditions, but of a changed economic level.'.

Certainly no group of men who in 1933 were ready, able and willing to buy the appellant's system and who were clothed in their right minds, would have paid, as the result of fair negotiations, any such sum for the portion of the road in North Dakota as was fixed by the Board. So that, while I agree that the court below, upon this record, was justified in denying the injunction prayed for, I am suffering from no illusions with respect to the great changes which took place in the value of all railway properties between the years 1929 and 1933. It may be impossible now for the Federal Courts to grant any relief to interstate carriers from overtaxation possibly resulting from honest mistakes or errors of judgment on the part of the taxing authorities of those States through which their lines run, but I believe that if interstate commerce by rail continues to be unreasonably overburdened with state taxes, either Congress or the courts will find some way to protect it. In this connection, the opinions of Judge Webster in Northern Pacific Ry. Co. v. Adams County, et al., (D. C. E. D. Wash.), 1 F. Supp. 163, and of Mr. Justice Brandeis in Nashville, Chattanooga & St. Louis Ry. v. Walters, et al., 294 U. S. 405, 55 S. Ct. 486, opinion filed March 4, 1935, are of interest."

We believe that a sounder line of reasoning is found in the language of Judge Webster in *Northern Pacific Ry. Co. v. Adams County*, in 1 Fed. Supp. 163, at pages 170 and 171, where the court said:

"There is no direct evidence in the record showing the methods which were employed by the tax commission in making the offending assessments. No member of the commission took the stand to explain the basis or bases upon which the commission acted in valuing and assessing the properties. No record of the commission shedding light on the method used was produced in evidence. It requires no argument to demonstrate that this attitude on the part of the commission does not foreclose all inquiry into the legality of their determinations. It merely serves to make necessary a different and obviously more difficult method of approach. In order to determine whether their valuations were properly made or are tinctured with constructive fraud arising out of gross excessiveness, it becomes necessary to consider whether, under any legally permissible method or combination of methods recognized by law for ascertaining value, their action can be upheld, as within the proper and legitimate exercise of their powers and discretion. This will be the standard of measurement which I shall apply in reaching my conclusions in this regard.

* * * * * *

Inasmuch as the Legislature of Washington has not defined specifically how railroad property shall be valued for taxation, I am of the opinion that the proper way of testing whether the action of the state tax commission can be upheld is to inquire whether under any legally authorized method or methods its determinations can be justified and sustained."

In the case just quoted from, the amount of over-assessment which was alleged (p. 168) was much less than the excess which we believe we have proven in this case, and yet the court found there that the assessments were "so grossly excessive as to give rise to a presumption of constructive fraud." (P. 185).

Both the trial court and the Circuit Court of Appeals overlooked the fact that this is not a case where the taxpayer has merely shown an actual value lower than the assessment, and where the court can still fairly presume that the Board may have had some different evidence before it, and may have honestly reached its conclusion by some rational though perhaps mistaken mental process. Here the evidence, like that in *Northern Pacific Ry. Co. v. Adams County,* supra, must convince any court that, to paraphrase the language of Judge Webster, "the action of the Board cannot be upheld under any legally permissible method or combination of methods recognized by law for ascertaining value * * * as within the proper and legitimate exercise of their powers and discretion." Where, as Judge Sanborn found, "no group of men who in 1933 were ready, able and willing to buy the appellant's system, and who were clothed in their right minds, would have paid as the result of fair negotiations, any such sum for the portion of the road in North Dakota as was fixed by the Board," we submit Judge Webster was right in his view of the law and that Judge Sanborn was mistaken in believing it to be "impossible now for the Federal Courts to grant any relief." "If interstate commerce continues to be unreasonably burdened with state taxes" as found by Judge Sanborn, we believe that the remedy is available under existing law, that Judge Webster correctly applied that remedy, and that no act of Congress and no change of law by the courts is required for relief in such cases. If the present law does not afford such a remedy, however, we certainly agree with Judge Sanborn that it is high time that some remedy was provided.

The defendants in this case did not rest upon the presumption in favor of the assessment but made a most elaborate attempt to justify it, through the evidence of Lyman Baker, a

tax specialist of Bismarck, North Dakota, and for thirteen years Deputy Tax Commissioner of the state, and now a general consultant (R. 144). Mr. Baker produced a voluminous set of tabulations and exhibits (R. 249-295), finding their culmination in Exhibit P (R. 277). This exhibit showed values for North Dakota computed by five different methods each of which indicated that the assessment for 1933 was from 15 to 25% in excess of actual value. The method used in subdivision 4 of this Exhibit P is the so-called five factor method described above, and is alleged by the state to be "the best and most accurate system of allocating the system value among the states" (Ans. par. I, K, R. 28, 29). This is the defendant's own pleading. By this method the actual value of the property in 1933 is computed at $63,307,629.00 while the assessment was $78,832,888.00. In other words, as a result of adopting the 1932 assessment for 1933, $15,500,000 or 24.52% was arbitrarily added to the actual value of the property as computed by the state itself, and with no foundation or pretense of justification. As quoted above, Mr. Baker also testified that he had been unable to find any method of computation that would produce a value equal to the assessment (R. 190).

The only defense offered against this confessed over-valuation is the naive contention that there had been no over-assessment in previous years, and that under the decisions of this court, the state has the right to make an irrational and highly excessive over-valuation if it is made for one year only and is not repeated. The court is asked to "presume" that the Board had some secret evidence known only to itself which it refused to disclose and which its own expert witness states that he was unable to discover, justifying the assessment and removing it from the domain of arbitrary action.

We grant that where a tract of land is assessed at $1000 and the owner offers proof, no matter how convincing, that it is actually worth only $750, the taxing authorities are not required to come forward and justify the value which they had found, but may rely upon the presumption that they had some evidence before them, that they attempted to act fairly upon it, and that the mistake if any was an error of judgment. But where they do not stand upon the presumption but attempt to justify the assessment by their own witness, who confesses that he has been unable to discover any evidence supporting the assessment or any rational process by which it could be reached, and where it is clearly shown that there is no possible computation by lawful methods which would produce the result, we submit that it must shock the conscience of a court of equity when it is asked to cling to the presumption that there was some evidence or some rational process, when the state's own witness confesses that he cannot find any, and when it is shown to be impossible that the Board could have had any such process or evidence.

It is true that many decisions hold that a mere showing by a taxpayer of over-assessment for a single year will not rebut the presumption. But we know of no instance where this or any other court has clung to the presumption of sufficient evidence in the face of an unsuccessful attempt by the state to justify the amount, and in the face of a confession by the state's own expert witness that he had been unable to discover any such evidence and that he knew of no method of computation by which the assessment could be justified, and that by his own best computation the assessment was $15,500,000 excessive.

We submit that an action is arbitrary if not based upon any evidence or any rational processes. Taking figures from the air or taking a number from a telephone book or a box car

would be arbitrary because it would not constitute even an attempt at a rational process or judgment. Writing down some amount by guess, even though in the best of good faith, if without any reason to believe that it is correct, is equally arbitrary. So is taking an assessment from some other year, after values are known to have changed. And even if the 1933 assessment were determined independently of that for 1932, the mere fact that it was in as large an amount as the 1932 assessment, and that no reduction was made, is in itself evidence of arbitrary action, in the face of defendants' admissions that the same methods of computation would show a shrinkage of $13,000,000 in value (Ans. paragraph L, R. 31, 32). This in itself is some evidence at least that the assessment was not the result of a rational mental process.

In this case the 1933 assessment was not made equal to that of 1932, in ignorance of the shrinkage in value which had occurred, because Exhibit Z-2 (R. 295-303), a statement by petitioner which was before the Board at the time of making its assessment, shows that full information had been given to the Board as to the actual shrinkage in value. For example, on page 297 of the record it appears that the Board had been advised that from 1931 to 1932 "the gross operating revenues of this company decreased 20%. The net railway operating income decreased 90%. The total market value of the Great Northern stocks and bonds decreased 35%." This statement contains full statistics in support of these figures.

It follows that the Board knew or had reason to know that a tremendous shrinkage in value had occurred since the assessment of 1932 was made; that the assessment of 1932 no longer represented 1933 values; and that there was no other evidence and no possible computation by which the 1933 assessment could have been computed as of that date. It follows neces-

sarily that in adopting the 1932 assessment for 1933, or in adopting an equal amount, the Board must have acted either without good faith or without the exercise of any rational mental process. Aside from the fact that the valuation of $63,000,000 computed by Mr. Baker was based upon pre-depression values, which no longer existed, and was based in large part upon values of property located outside the state, the fact that the assessment was $15,000,000 beyond what could be computed even by these unjustifiable methods in itself proves arbitrary action.

The Circuit Court of Appeals states that there was "a decided improvement in stock and bond prices (generally and as to appellant) in 1933 prior to the assessment; and that there had been slight reductions (in assessments) in 1931 and 1932" and "that it is not unusual for the Board to use approximately the same amount for successive years." The court concludes "it may well be, in view of this situation, that the Board might honestly deem its reduction of 1932 (5%) to have sufficiently taken care of the effect on value of the depression covering 1932 and passing into 1933—especially in view of apparent improvement in conditions in 1933."

The improvement in stock and bond prices from 1932 to 1933 upon which the court lays so much stress, is an improvement from $296,301,177 to $305,709,875, an increase of a little over 3% (Ex. 18, R. 243). In view of the fact that the 1927 to 1929 figures upon which the 1932 assessment had largely been based were more than 100% above the 1932 figures, the suggestion that this disastrous shrinkage had been sufficiently met by an assessment reduction of 5%, and that the necessity for any further reduction had been removed by a 3% increase in stock and bond prices, can hardly have been intended seriously, and the fact "that it is not unusual for the Board to use approximately

the same amount for successive years" cannot seriously be presented as a justification for ignoring a $15,000,000 shrinkage in value.

In view of the fact that the commercial value of the property as indicated by current earnings and stock and bond prices was not over $25,000,000; that no men "who were clothed in their right minds" would pay anything like the amount of the assessment for the property; and that the defendants' expert witness testified that he has been able to find no evidence or method of computation by which the assessment can be justified, we submit that this assessment would have to be canceled, even though there were no evidence whatever that boom period prices had been used or that out-state values had been assessed.

F

The economic emergency does not justify the violation of the statute requiring the assessment of property at its full and true value in money.

The defendants claim that an economic emergency existed, that stocks had lost their value, that there was a flight from securities, that farms no longer had any income, that the earnings of all property had practically disappeared, and that the board was, therefore, not obliged to give the usual weight to current earnings and stock and bond prices or to follow the usual formulae in determining values.

Assuming for the sake of the argument that these economic conditions would be sufficient justification for not basing the value of the property on its 1932 earnings of only $1,292,000 (which would give the system a value of about $20,000,000 and North Dakota about three or four million dollars) or even that

they would be sufficient justification for not reducing the assessment as low as $25,000,000 as indicated by current stock and bond prices and three years earnings, still it does not follow that the Board is acting within the zone of reason or permissible discretion in totally ignoring depreciated values or in trebling the actual current value of the property, and in refusing to give any recognition whatever to the shrunken depression values and to the complete disappearance of boom period values. Neither the Board nor the Court should absolutely blind itself to these changed conditions.

The law requiring assessment at the true and full value in money still remained upon the statute books. And no economic emergency will justify an administrative tribunal in setting up its own opinions as to the requirements of the public welfare, above the requirements of law.

In *Home Bldg. & Loan Assn. v. Blaisdell*, 290 U. S. 398 at 425, 54 S. Ct. 231, this court said:

> "Emergency does not create power. Emergency does not increase granted power or remove or diminish the restrictions imposed upon power granted or reserved."

In *Ex parte Milligan*, 4 Wall. 2, at 121, this court said:

> "The Constitution of the United States is a law for rulers and people, equally in war and in peace, and covers with the shield of its protection all classes of men, at all times, and under all circumstances. No doctrine, involving more pernicious consequences, was ever invented by the wit of man than that any of its provisions can be suspended during any of the great exigencies of government. Such a doctrine leads directly to anarchy or despotism, * * *"

In *A. L. A. Schechter Poultry Corp. v. U. S.*, 295 U. S. 495, 55 S. Ct. 837 at 842, this court said:

"We are told that the provision of the statute authorizing the adoption of codes must be viewed in the light of the grave national crisis with which Congress was confronted. Undoubtedly, the conditions to which power is addressed are always to be considered when the exercise of power is challenged. Extraordinary conditions may call for extraordinary remedies. But the argument necessarily stops short of an attempt to justify action which lies outside the sphere of constitutional authority. Extraordinary conditions do not create or enlarge constitutional power. The Constitution established a national government with powers deemed to be adequate, as they have proved to be both in war and peace, but these powers of the national government are limited by the constitutional grants. Those who act under these grants are not at liberty to transcend the imposed limits because they believe that more or different power is necessary."

It follows from these decisions that the Board was still obliged to comply with the law, and to assess the property at its actual money value. And even assuming that there was a *potential* value above the current indicated value, based upon the hope of a return to normal times, and that the Board, would, therefore, have been justified in assessing the property at more than its current indicated value, it does not follow that it was justified in shutting its eyes entirely to the fact that even the highest possible potential value based upon the hope of a return at some indefinite time in the future to normal business conditions, must be very much less than the inflated boom period values of 1929. We submit that even in the face of all of the emergencies pointed out by the defendants, it was not the exercise of a rational mental process for the Board to continue an assessment in 1933 which was three times the current value, which could not be justified even by the use of five

years earnings and stock and bond prices, and which was only 1% less than the boom period assessment of 1929.

And even if we are entirely mistaken in this, and even if the Board were fully justified by the emergency in continuing boom period assessments in effect, it would not be justified on that ground in continuing to assess properties located in other states. The "economic emergency" argument does not even pretend to justify the state of North Dakota in assessing terminals located in Minnesota and Washington, which the State had done, not only in 1933, but for many previous years.

CONCLUSION

In conclusion we submit that the use of pre-depression prices and of mileage prorates in making the assessment is not only proven but admitted; that these methods necessarily assess values which have ceased to exist, and properties in other states, and treble the actual current value of the property; that after computing a valuation by such methods, the addition or subtraction of a few dollars before placing the amount on the assessment rolls, does not immunize the assessment against attack; that the use of such methods is not within the permissible range of discretion of taxing officers; that an attempt by the taxing officers to justify the assessment which ends in failure and in a confession that it cannot be justified, and that it is $15,000,000 in excess of the fairest computed values is in itself sufficient proof that the assessment was either arbitrary, irrational, or fraudulent; and that it is not necessary for the taxpayer to submit to such assessments repeatedly, before the courts can grant relief.

Petitioner has already paid 60% of the taxes levied against the assessment in question (R. 81). A temporary injunction

has been issued restraining the collection of the balance of the taxes *pendente lite.*

We submit that the assessment which was levied in 1933 was wholly invalid; that further taxes levied under that assessment cannot lawfully be collected; and that the injunction against the further collection of such taxes should be made permanent.

We believe that the court should find that no assessment can be made under any proper or lawful methods in excess of 80% of the present assessment upon which we have already paid taxes, and submit that the making of a substitute assessment for any larger amount should be enjoined.

Respectfully submitted,

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November 2, 1935.

APPENDIX A.

EXTRACTS FROM SEVENTH BIENNIAL REPORT OF THE NORTH DAKOTA TAX COMMISSIONER TO THE GOVERNOR AND LEGISLATURE FOR THE FISCAL YEARS 1923 AND 1924.

Pages 55 and 56.

"The assessment of public utility property in this state has been a matter of more or less general discussion for a number of years, and consequently, it seems advisable to set forth briefly the method of valuation used in this state and to discuss some of the problems in connection with the making of an assessment of this class of property. This discussion will deal primarily with the assessment of railroad property, as it is the only important class of public utility property in this state. Section 2242, Compiled Laws of 1913, requires the state board of equalization to assess annually at its actual value the franchise, roadway, roadbed, rails and rolling stock of all railroads operating in this state, and also requires that in estimating the value of such railroads, branches and sidetracks thereof, the board shall be governed by the same rules as are provided for the guidance of county and township assessors in valuing other property.

The general taxation laws of this state require that all taxable property must be valued and assessed by the assessor at full and true value. The term full and true value is defined as the usual selling price at the place where the property to which the term is applied is located at the time of the assessment, being the price which could be obtained therefor at private sale and not at a forced public auction sale. The full and true value of any class of property is also defined as the amount of money which the average man desiring to own it

would be willing to pay for it for its ordinary use and the amount the man owning it would be willing to accept in payment for it; in other words, the full and true value is the usual selling price or market price.

Railroads are not bought and sold as a unit under ordinary circumstances and consequently the value of railroad property is ordinarily found by the use of one of three methods; (1) by capitalizing the average net operating income of a railroad for a five year period, or (2) by ascertaining the average total market value of its stocks and bonds for a five year, one year or lesser period, or (3) by a combination of both of these methods."

Page 58.

"The valuation figures which the state tax department placed before the state board of equalization for the year 1924, gave a composite method of valuation. The determination of the system value of a railway was made on the basis of capitalizing net earnings at 6 per cent for a one year, three year and five year period and using stock and bond values for a one year and five year period. The apportionment of system valuation was made to North Dakota on the basis of five factors:

(1) The proportion which all track mileage (including main line, branch line, second tracks, sidetracks, etc.) within North Dakota bears to the all track mileage of the system.

(2) The proportion which gross earnings within North Dakota bears to system gross earnings.

(3) The proportion which car and locomotive mileage within North Dakota bears to system car and locomotive mileage.

(4) The proportion which revenue ton and passenger mileage within North Dakota bears to system revenue ton and passenger mileage.

(5) The proportion which the physical value, that is, the cost of reproduction of the property in North Dakota bears to system cost of reproduction of the property.

The basis of apportionment used is a composite basis. The average of the five ratios above given were applied to the estimated system value of the railroad."

APPENDIX B.

EXTRACTS FROM TENTH BIENNIAL REPORT OF THE NORTH DAKOTA TAX COMMISSIONER TO THE GOVERNOR AND LEGISLATURE FOR THE BIENNIAL PERIOD

July 1, 1928 to June 30, 1930.

Page 50.

"It should be clearly understood that whatever erroneous or incorrect assessments develop in connection with the assessment of public utility property are the responsibility of the tax commissioner and not the state board of equalization. The four ex-officio members of the state board of equalization must depend upon the work of the tax department in connection with the assessment of public utilities. It is impossible for ex-officio board members in the few days devoted to board meetings in the month of August to value the property of hundreds of public utilities located in approximately 2,000 taxing districts throughout the state. The state board is compelled to look to the tax commissioner for guidance and to depend upon

his judgment and the work of his department in the assessment of public utility property. The tax commissioner, however, in order to do the requisite work preliminary to assessment by the state board must have the statutory authority to require utility companies to make such reports as he may need and he also must have at his disposal the necessary funds to pay the traveling expenses incidental to plant inspections and appraisals. In this connection it may be stated that utilities have voluntarily complied with every request that the tax department has made and have manifested a fine courtesy and willingness to cooperate."

Page 51.

"It is generally recognized that a direct commercial or market valuation of that part of a railroad which lies within a given state is impossible and that it is first necessary to determine the value of a railroad as an entirety before it is possible to logically assign a value to that portion within a given state. It has been the practice of the state tax department to determine the value of each railroad subject to taxation in North Dakota as an entirety and then to assign to North Dakota its proportionate share of the system valuation, on the basis of approved factors of allocation.

The market value of railroad property is ordinarily estimated or determined by the use of one or both of the two following methods:

(a) By finding the aggregate average market value of the stocks and bonds of the company as determined by the average price paid by the public for its various securities over a reasonable period of time, or

(b) By capitalizing the average amount earned on the operating property over a period of years at a reasonable rate of return."

Pages 52 and 53.

"In connection with the use of the stock and bond method of valuation of railroad property, it is necessary to distinguish between the value of the property actually used for railroad purposes and the value of other property owned by the railroad company. Such other property, if it lies within the state of North Dakota, will be separately assessed; if it lies outside the state of North Dakota, it is not a proper subject for taxaiton by North Dakota and not a part of the system valuation of the operating property of the railroad and, consequently, must be excluded in determining what proportion of stock and bond values is assignable to operating property.

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It has been the practice of the state board of equalization and of the state tax department to determine railroad valuations on the basis of stock and bond values and capitalized net operating income, giving weight to each of these indices of value.

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ALLOCATION OF VALUATION TO THE ASSESSING STATE. The most serious problem which arises in connection with the assessment of an interstate railroad property is to determine what proportion or amount of the total value of the system lies within the particular state. It is generally conceded that it is impossible to determine the value of a part without reference to the value of the whole, consequently, all taxing authorities and boards in valuing interstate railroad companies first find the value of the whole and then attempt to determine the value of the part which lies within a particular state.

The factors of allocation which are used by the tax department in North Dakota are:

1. All track mileage.
2. Gross earnings.
3. Car mileage.
4. Traffic units.
5. Physical value.

APPENDIX C.

Extract from Pages 5 and 6 of Report of Committee on Interstate and Foreign Commerce of the House of Representatives, 74th Congress, First Session, Report No. 1560, dated July 22, 1935, recommending Passage of H. R. 3263.

THE REASONS WHY THIS BILL SHOULD BE ENACTED IN THE PUBLIC INTEREST

1. If the railroads at one time had, they no longer have a monopoly in the transportation field. Ships and trucks are in position to handle a large part of the traffic that formerly moved exclusively by rail. Since 1920 there has been a tremendous growth of competitive forms of transportation. The intercoastal steamship lines now concededly have a practical monopoly of all traffic transported between the seaboards with the exception of perishables, and reach far inland on westbound traffic, charging lower rates on traffic originating at the interior than charged on traffic at or in the vicinity of the port. This has resulted from the long-and-short-haul provision of the fourth section, which evidently the Commission has interpreted to be the meaning of its provisions as a matter of congressional

policy. Foreign steamships are prevented by law from engaging in domestic traffic.

Principally through Government expenditures providing rights-of-way, large amounts of traffic have been diverted to competitive forms of transportation on inland waterways including rivers and canals. The Government itself engages in a competitive operation on the Mississippi River.

Since 1920 the competition of millions of trucks and busses throughout the country has developed, as has also the competition of pipe lines transporting petroleum, gasoline, and natural gas, supplanting other forms of fuel including coal. Electric lines ship "coal by wire."

The Interstate Commerce Commission itself, in a decision rendered in July, 1933, *General Rate Level Investigation, 1933*, 195 I. C. C. 5, at pages 70 and 71, stated that in 1931 they believed that the depression was the principal cause of the then unfavorable condition of railroad revenues and credit, but that competition of other forms of transportation has grown to such formidable proportions that the opinion expressed in 1931 no longer portrays the situation. The Commission there said:

> "Formerly it was thought that competing motor carriers were taking and would take principally short-haul less-than-carload traffic, and that water carriers would take principally low-grade freight. Time has disproved both of these beliefs. Water carriers are now taking much high-grade long-haul traffic. Trucks are handling less-than-carload freight over long distances and also vast quantities of freight which heretofore has moved on the railroads in carloads, principally commodities which have been most profitable to the railroads."